

Master Builders Australia

Foreign Direct Investment

In Australian Real Estate

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1 Introduction

- 1.1 Master Builders Australia is the nation's peak building and construction industry association which was federated on a national basis in 1890. Master Builders Australia's members are the Master Builder state and territory Associations. Over 124 years the movement has grown to over 32,000 businesses nationwide, including the top 100 construction companies. Master Builders is the only industry association that represents all three sectors, residential, commercial and engineering construction.
- 1.2 The building and construction industry is a major driver of the Australian economy and makes a major contribution to the generation of wealth and the welfare of the community, particularly through the provision of shelter. At the same time, the wellbeing of the building and construction industry is closely linked to the general state of the domestic economy.

2 Overview

- 2.1 This inquiry commences on shaky foundations – very little of a concrete nature is known about the incidence, pattern and stock of foreign investment in Australian real estate.
- 2.2 The best available information appears to suggest:
- foreign buyers account for between around 4 and 7 per cent share of overall demand for established residential properties; and,
 - at least 5 to 8 per cent, and likely not more than 12 or so per cent, of overall demand for new residential properties in recent years.
- 2.3 Foreign buyers add directly to the housing stock (buying new residential property), and indirectly to the extent their purchases of existing properties facilitates the vendors of those properties subsequently purchasing other new properties (as can be the case with down-sizers).

- 2.4 Any increasing demand by foreign buyers for Australian residential property also likely reflects a rational response to a number of positive economic, legal and political factors, such as:
- Australia has an international reputation amongst foreign investors as having low political, economic and/or legal risk, which adds to our appeal for foreign investors; and,
 - the strong interest by foreign investors in Australian real estate is a vote-of-confidence in the Australian economy, and its future.
- 2.5 Anecdotal evidence available to Master Builders from consultations with our members suggests foreign buyer activity is expanding housing supply in Australia
- 2.6 Insofar as foreign buyers of Australian real estate may be adding to the demand-supply imbalance, **the appropriate policy response is not to impede demand but to reform and liberalise the supply side of the Australian housing market.**
- 2.7 Key elements of such housing supply reforms are set down in Master Builders National Housing Affordability Agenda (NHAA), which advocates, inter alia:
- the Federal Government to provide ex post 'competitive, efficiency dividend' payments to the State, Territory and Local Governments for delivering housing supply policy outcomes against key performance metrics;
 - local governments to develop individual Land Release Plans, and associated marketing strategies, for their own jurisdictions over a ten year ahead rolling time horizon;
 - the realisation of a genuine, rigorous, enforceable, transparent and uniform building code and regulatory system;
 - a review of the impact of stamp duties on residential property, and alternate approaches to revenue-raising, recognising such transaction costs are inefficient taxes and impede movement within the housing and labour markets;

- the annual publication of a rigorous stocktake of the approaches to developer/infrastructure charges by all local governments in Australia; and,
- commitments by all governments to deliver substantive outcomes which will raise labour productivity growth rates, including greater flexibility in labour markets emphasising genuine enterprise bargaining.

3 Terms of reference

3.1 The House of Representatives Standing Committee on Economics on 19 March 2014 initiated an inquiry into foreign investment in Australian real estate (Parliament of Australia, 2014)

3.2 In announcing the inquiry, the Committee observed, inter alia:

- foreign investment in Australian real estate should increase Australia's housing stock;
- such investment should increase the supply of new housing, and benefit the local building industry and its suppliers;
- foreign investors can seek approval to purchase new dwellings and vacant land for residential development; and,
- while foreign investors cannot generally buy established dwellings as investment properties or homes, temporary residents can apply to purchase one established dwelling to use as their residence while in Australia.

3.3 The specific terms of reference for the Inquiry require the Committee to examine:

“the economic benefits of foreign investment in residential property;

whether such foreign investment is directly increasing the supply of new housing and bringing benefits to the local building industry and its suppliers;

how Australia's foreign investment framework compares with international experience; and,

whether the administration of Australia's foreign investment policy relating to residential property can be enhanced.”

3.4 The Committee is required to report by mid October 2014.

4 Foreign investment in Australian real estate

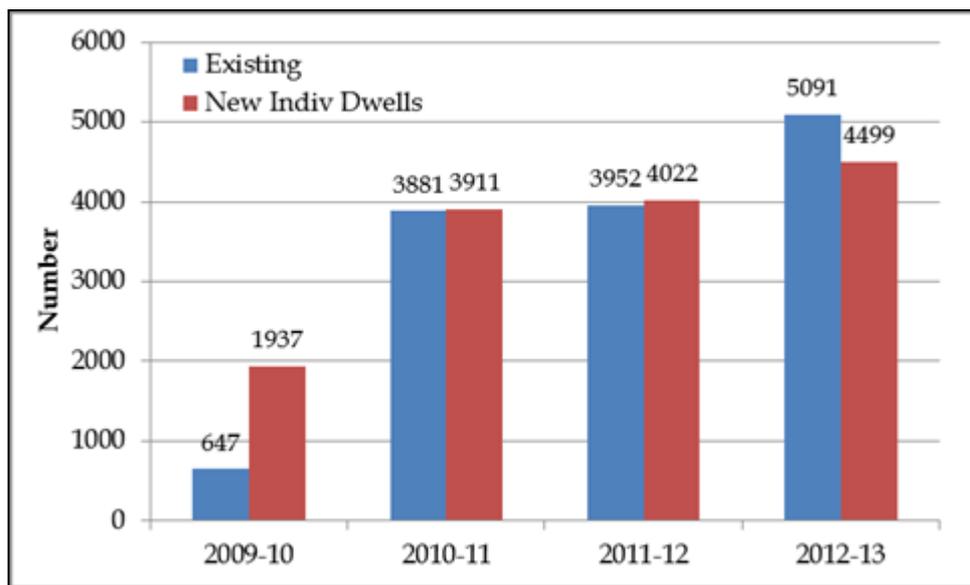
4.1 This inquiry commences on shaky foundations – very little of a concrete nature is known about the incidence, pattern and stock of foreign investment in Australian real estate.

4.2 Official data on foreign investment in real estate is, unfortunately, published only at the aggregate level, and does not appear to allow disaggregation by the country-of-origin of the investor (FIRB, 2013).

4.3 However, an overview of some of the aggregate data, and simple data analyses, provides some modest insight into broader patterns of foreign investment in Australian real estate.

4.4 Graph 1 reports the number of applications approved by the Federal Government for the purchase of individual existing and new dwellings by foreign nationals over the four financial years up to and including 2012/13.

Graph 1: Foreign Investment Approvals: Number

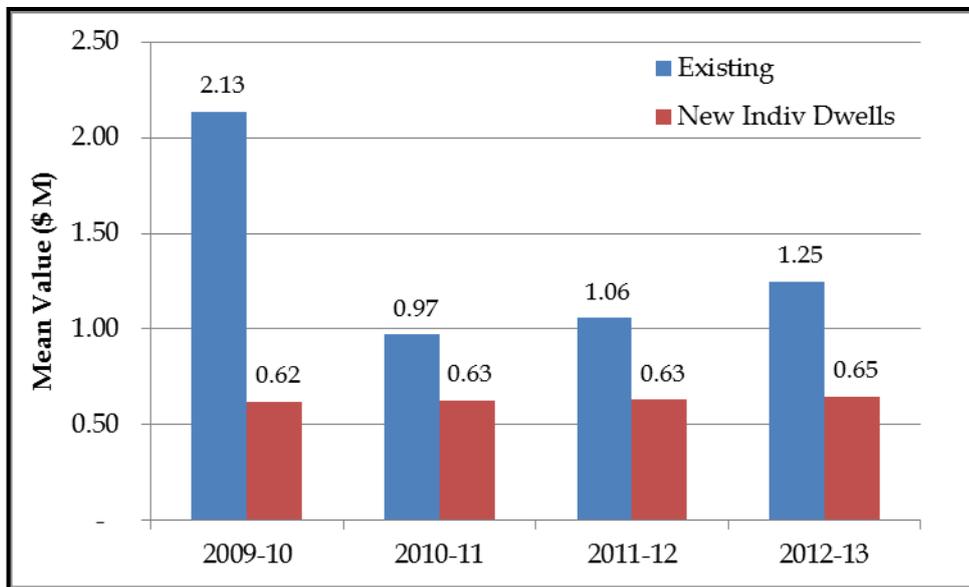


4.5 Several messages stand out from a review of Graph 1, inter alia:

- the overall number of approvals for the purchase of individual existing dwellings jumped markedly between 2009/10 and the 2010/11; and,
- while the number of approvals for individual new dwellings exceeded that for existing individual dwellings in 2009/10, by 2012/13 the roles were reversed (although with a slimmer margin).

4.6 Graph 2 reports the average value for these purchases.

Graph 2: Foreign Investment Approvals: Average Value



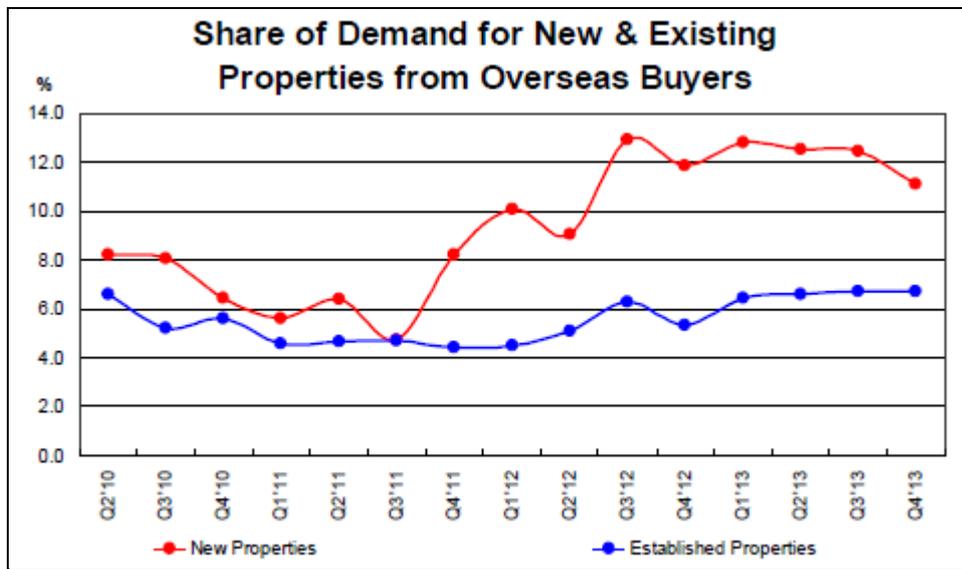
4.7 Several messages stand out from a review of Graph 2, inter alia:

- the average value of approvals for the purchase of individual existing dwellings by foreign nationals has risen fairly modestly since 2010/11, with such properties being at the 'higher priced' end of the residential property market; while,
- the average value of purchases of individual new dwellings has remained reasonably stable over the four years to 2012/13, with such properties also at the 'higher priced' end of the residential property market.

4.8 The average price of residential dwellings in Australia was \$498,800 in 2012/13 (ABS, 2014).

- 4.9 Market research by National Australia Bank (NAB, 2014) provides another useful insight into the incidence of foreign demand for Australian residential property.
- 4.10 Graph 3 (taken from NAB, 2014) reports the share of demand for new and existing properties coming from overseas buyers.
- 4.11 The blue line (with circular markers) refers to established properties, while the red line (with square markers) refers to new properties.

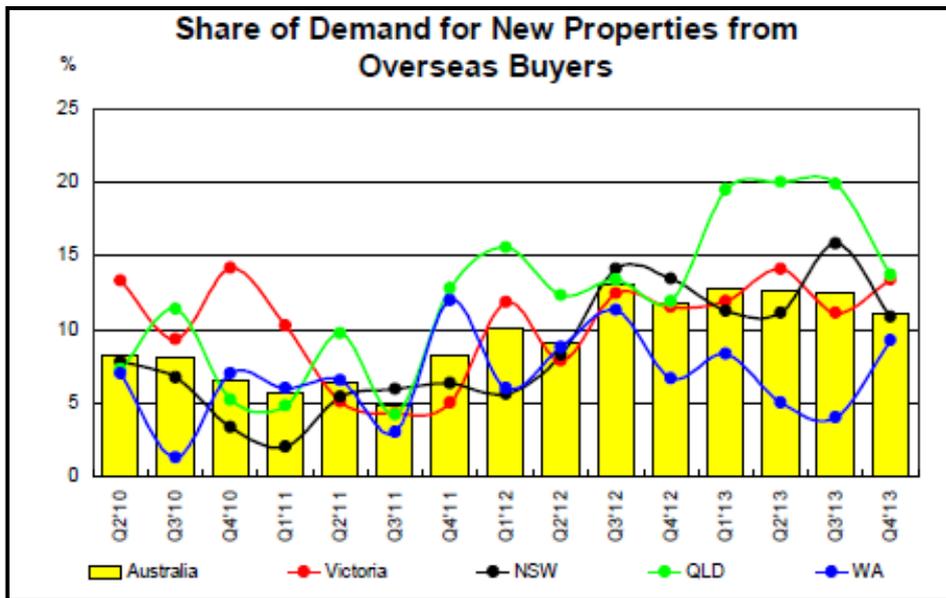
Graph 3: Foreign Demand for Australian Residential Property



- 4.12 Several messages stand out from a review of Graph 3:
- looking first at the blue/ circle marked line, foreign buyers have accounted for between around 4 and 7 per cent share of overall demand for established properties in the almost 4 years under review;
 - turning to the red/square marked line, foreign buyers have accounted for between around 5 and 8 per cent of overall demand for new properties in the years 2010 and 2011, with the share jumping into the 12 to 13 per cent share range in much of 2012 and 2013.

- 4.13 Taken together, these messages paint a picture of foreign buyers adding directly to the housing stock (buying new residential property), and indirectly to the extent their purchases of existing properties facilitates the vendors of those properties subsequently purchasing other new properties (as can be the case with down-sizers).
- 4.14 Foreign demand for new residential property is not evenly distributed across the nation, as Graph 4 shows.

Graph 4: Foreign Demand for Australian Residential Property II



- 4.15 Focusing on the 2012 – 13 period, we can see, inter alia, foreign demand accounts for:
- a larger share of demand for new properties in Queensland, relative to the national average;
 - around the same shares of demand for new properties as the national average in both NSW and Victoria; and,
 - generally well below the national average share of demand for new properties in Western Australia.
- 4.16 (The NAB survey does not report comparable results for existing residential property.)

4.17 Credit Suisse, a global private financial institution, has also examined the nature and the incidence of Chinese investment in Australian residential property (Credit Suisse, 2014). Amongst the main findings of their analysis are:

- Chinese buyers are currently purchasing around \$A 5 billion of Australian residential property annually;
- this figure accounts for around 12 per cent of new housing supply in Australia, ranging from a low of around 2 per cent in Tasmania and the Northern Territory to highs of 14 per cent in Melbourne and 18 per cent in Sydney;
- purchases of Australian residential property by Chinese buyers could rise by a further \$A 44 billion over the next seven years;
- Credit Suisse believes these estimates are conservative, and may well understate the extent of the Chinese footprint in Australian residential property;
- where a Chinese buyer purchases an existing residential property for redevelopment, such projects are usually done with little or no debt;
- Chinese buyers are not likely to be driving up residential property prices nationally, although they are “a much more powerful force in Sydney and Melbourne” (Credit Suisse, 2014: 4); and,
- they also major buyers of property in other cities around the world, such as New York, Los Angeles, London, and Vancouver.

4.18 Media reporting of the incidence and pattern of foreign investment in Australian real estate is at best sparse.

4.19 Nevertheless, some of the messages coming from the better media reporting (see for example, Cranston and Thistleton 2013) include:

- there is little hard data around about the incidence and pattern of foreign investment in Australian real estate cross-tabulated by the nationality of the investor;

- the share accounted for by any particular foreign nationality is hard to determine;
- foreign investor interest in the Australian real estate market is not unique, but is being experienced in a number of major cities around the world (eg Auckland, London, Los Angeles, Singapore, Vancouver);
- the declining value of the Australian dollar on foreign exchange markets improves the appeal of Australian assets generally for any rational foreign investor;
- Australia has an international reputation amongst foreign investors as having low political, economic and/or legal risk, which adds to our appeal for foreign investors;
- the growth in foreign investment in Australian real estate would appear to correlate with the growing number of foreign students in Australia (who merely may be looking for somewhere to live whilst studying here (see also FIRB, 2013: 28));
- foreign investors in Australian real estate, especially for new developments, are 'cashed up', and are not constrained by the lending policies and practices of Australian central and lending banks (as may be the case with prospective Australian property developers);
- the names and the visual image of ethnicity is not necessarily a good guide to an investors nationality: an 'Asian' buyer could well be an Australian citizen; a 'Caucasian' buyer could well be a foreign national; and,
- the strong interest by foreign investors in Australian real estate is a vote-of-confidence in the Australian economy, and its future.

5 Previous inquiries

- 5.1 Master Builders notes there have been several important inquiries into, and reviews of, barriers to housing supply and affordability challenges over the past few years.
- 5.2 Three of the most prominent of these inquiries/ reviews were:
- the Senate Select Committee Inquiry into Housing Affordability in Australia (conducted during 2008);
 - the Housing Supply and Affordability Report (HSAR) prepared for the Council of Australian Governments (COAG; delivered in 2012); and,
 - the Senate Economics References Committee Inquiry into Affordable Housing (currently underway; due to report before the end of June 2014).
- 5.3 The Federal Parliament conducted an inquiry into barriers to home ownership in Australia during the 2008-10 Parliament.
- 5.4 The inquiry was undertaken by the Senate Select Committee on Housing Affordability in Australia, which published its final report in June 2008 (Parliament of Australia, 2008).
- 5.5 Key terms of reference for the inquiry were considerations of:
- the taxes and levies imposed by State and Territory governments;
 - the rate of release of new land by State and Territory governments;
 - proposed assistance for first home owners by Federal, State and Territory Governments, and their effectiveness in the absence of increased supply;
 - the role of all levels of government in facilitating affordable home ownership;
 - the effect on the market of government intervention in the housing sector, including planning and industrial relations laws; and,
 - the contribution of home ownership to retirement incomes.

5.6 Master Builders made an expansive submission to this inquiry (Master Builders, 2008).

5.7 The main themes emphasised by Master Builders in that submission include:

- Australia has suffered for more than a decade from policy neglect by all levels of government;
- there was an urgent need to develop a unified national strategy to combat the crisis in housing affordability;
- the critical policy priority must be to deal with the problem of the lack of housing supply. As such, the policy must adopt a 'supply side first' response;
- the appropriate policy response involved a package of meaningful reforms which had to include:
 - improved land release programs, and planning approvals processes;
 - a review of developer (also known as infrastructure) charges, with increased funding for such infrastructure from general revenue sources; and,
 - the replacement of stamp duties with less distorting taxes.

5.8 The Committee in its final report made a number of important findings, including:

- there was a significant housing affordability problem in Australia;
- housing affordability pressures impact both prospective home buyers and renters;
- housing affordability pressures reflect the interaction of strong demand and limited supply;

- the shortfall in housing supply reflected three key factors, namely:
 - planning processes at State and Local Government levels were too complex, too costly, too lengthy in time and frequently too uncertain, which in turn impeded land release and added to the cost of housing supply which was ultimately borne by the home buyer;
 - developer/ infrastructure charges can be excessive and act to restrict supply; and,
 - there was a shortage of skilled labour in the construction industry, which was likely to prevent the industry from meeting projected housing and other building and construction demands.
- stamp duties are inefficient taxes, a burden on home buyers and discourage people from relocating to more appropriate housing types (eg 'upsizing' or 'downsizing') as their needs change (eg family growth or retirement by 'empty nesters') and,
- the housing affordability problem was essentially structural, rather than cyclical, meaning policy responses must include longer term solutions, one of which was encouraging regional decentralisation/ development.

5.9 The Housing Supply and Affordability Report (HSAR) provided to the Council of Australian Governments (COAG; COAG, 2012) made findings which largely echoed those of the Senate Select Committee report,

- an indicator of government failure in delivering meaningful progress in the intervening period in actioning barriers to improving housing affordability in Australia.

5.10 Key findings of the HSAR include:

- builders and property developers face significant delays, uncertain time frames and unpredictable regulatory burdens in supplying new land and housing to the market place, which in turn add to the costs of housing supply;

- planning approvals processes imposed by State and Local Governments add to housing supply costs, and so reduce housing supply and overall housing affordability;
- infrastructure supply charges imposed on property developers lacked consistency, transparency and predictability. Where such imposts are applied they should be efficient, transparent, accountable, predictable and equitable; and,
- government housing programs should be reformed to improve housing affordability for low income households and the effectiveness of such programs for those in greatest housing need; and,
- The Senate Economics References Committee initiated an inquiry into Affordable Housing, which is due to report before the end of June 2014.

5.11 In our submission to that inquiry, Master Builders noted, inter alia:

- as a nation, Australia has one of the highest levels of housing unaffordability in the world – being second only to Hong Kong on global league tables of housing unaffordability;
- in our major capital cities, housing is at best ‘not affordable’ in Brisbane, Hobart, Canberra and Darwin, and at worst ‘severely unaffordable’ in Sydney, Melbourne, Adelaide and Perth; and,
- a growing number of our major regional areas – such as the Sunshine Coast and the Gold Coast in Queensland, Coffs Harbour and Newcastle in NSW, Mandurah in Western Australia, and Geelong in Victoria - are also ‘severely unaffordable’.

5.12 Master Builders also recognised while there had been some indicators showing an easing in housing affordability pressures, this situation is unlikely to be sustained for a number of reasons, including:

- government failure to deliver sufficient reduction in structural barriers to housing supply (most notably land release), especially at State and Local Government levels;

- the easing cycle in interest rates in Australia has likely reached its trough; and,
- the likely continuation of healthy rates of population growth in general, and from net overseas migration in particular, which will add to housing demand.

5.13 Master Builders called on Federal, State/Territory and Local Governments, working together, to commit to and deliver, a bold and comprehensive National Housing Affordability Agenda (NHAA), key elements of which include:

- tangible outcomes in improving the efficiency, and the supply-side efficiency in particular, of the Australian housing market;
- local governments to develop individual Land Release Plans, and associated marketing strategies, for their own jurisdictions over a ten year ahead rolling time horizon;
- the realisation of a genuine, rigorous, enforceable, transparent and uniform building code and regulatory system;
- a review of the impact of stamp duties on residential property, and alternate approaches to revenue-raising;
- the annual publication of a rigorous stocktake of the approaches to developer/infrastructure charges by all local governments in Australia; and,
- commitments by all governments to deliver substantive outcomes which will raise labour productivity growth rates, including greater flexibility in labour markets emphasising genuine enterprise bargaining.

6 Reform priorities

- 6.1 The Federal, State and Territory, and Local Governments need to recommit to the goal of improving housing supply and housing market efficiency, and to working together to achieve this critical priority objective.
- 6.2 Meaningful and sustainable improvements in housing supply can be achieved by the Federal, State and Territory, and Local Governments, individually and collectively through COAG, committing to a common and National Housing Affordability Agenda (NHAA).
- 6.3 The Federal Government, through COAG should provide ex post ‘competitive, efficiency dividend’ payments to the State, Territory and Local Governments for delivering housing supply policy outcomes against key performance metrics including:
- adequate supply of ‘releasable’ land, whether ‘greenfield’ or ‘brownfield’;
 - streamlined and more efficient building and planning approvals processes;
 - agreed ‘master plans’ covering urban and regional infrastructure plans and urban consolidation;
 - adherence to the Building Code of Australia, and removal of State and Local Government variations; and,
 - reforms to infrastructure (also known as ‘developer’) charges.
- 6.4 The performance outcomes to be achieved, and the key indicators to be used to measure those outcomes (as distinct from endeavours) should be determined by an independent panel drawn from key stakeholders, in particular representatives of the building and construction industry.
- 6.5 The achievement of these outcomes/ indicators, and the apportionment and quantum of the ‘competitive, efficiency payments’ across the State, Territory and Local Governments would be assessed by an independent panel comprising commissioner or the equivalent level personnel from the Commonwealth Grants Commission, the Productivity Commission and the Federal Department of Finance.

- 6.6 To be clear, the onus of proof for the payment of competitive, efficiency dividends will lay with the State, Territory and Local Governments.
- 6.7 The other key elements of a NHAA should also include:
- local governments to develop individual Land Release Plans, and associated marketing strategies, for their own jurisdictions over a ten year ahead rolling time horizon;
 - the realisation of a genuine, rigorous, enforceable, transparent and uniform building code and regulatory system;
 - In this context, there is strong support within the building and construction industry for making the National Construction Code (NCC) free-on-line, and better integration of relevant Australian Standards into such documentation.
 - a review of the impact of stamp duties on residential property, and alternate approaches to revenue-raising, recognising such transaction costs are inefficient taxes and impede movement within the housing and labour markets;
 - the annual publication of a rigorous stocktake of the approaches to developer/infrastructure charges by all local governments in Australia; and,
 - commitments by all governments to deliver substantive outcomes which will raise labour productivity growth rates, including greater flexibility in labour markets emphasising genuine enterprise bargaining.
- 6.8 The primary policy challenge for the Federal, State, Territory and Local Governments in Australia is in the first instance to facilitate an efficient Australian housing market.

- 6.9 An efficient housing market would have a number of features, including:
- a supply-side which is responsive to changes in demand-side drivers;
 - one not burdened by distortions to market prices (the principal method by which housing demand signals are transmitted to housing suppliers);
 - regulatory, as well as subsidy and taxation interventions, which distort and reduce the efficient operation of the housing market, are minimal, transparent and based on sound economic principles; and,
 - where governments and other regulators wish to achieve social and other policy objectives in the housing sector, these outcomes be pursued through directly relevant policy instruments and in a manner which has the least possible distortionary impact on the housing market.
- 6.10 The Council of Australian Governments (COAG), and the Federal Government in particular, should develop and first report on key performance indicators of housing market efficiency, the Productivity Commission (PC) should develop, and publish annual updates of, the housing market efficiency performance indicators; engaging with other, and third party agencies in government and the private sector to progress this work to ensure its depth and relevance for housing policy-makers and those in housing market practice.
- 6.11 All Local Governments in Australia develop individual Land Release Plans which identify and provide an indicative forward schedule of 'brownfield' and 'greenfield' land over a rolling 10 year ahead time horizon which could progressively be made available for residential housing development.
- These Land Release Plans would, inter alia, identify specific tracts of land within own-jurisdictions, set down timelines for their prospective availability for residential development, any regulatory or other requirements which may impede the land release process, generally and for specific tracts of land, and nominate those tracts which would be 'development-ready' within five years; and,

- the respective State/Territory Governments would be required to subject these Land Release Plans to competitive benchmarking and other performance evaluations, whom in turn would be subject to benchmarking and evaluation by the Productivity Commission as part of the regular Report on Government Services (ROGS) processes.
- The Federal, State and Territory Governments champion a national uniform and enforceable building code and regulatory system to ensure the development and continuation of an efficient and competitive building industry;
- continue to play an active leadership role in the ongoing development and refinement of the Building Code of Australia (BCA) as the central document that specifies a national set of building requirements consistently across Australia; and,
- work to change the current system to introduce further controls on local governments so they no longer have a free hand to add new regulations and conditions on buildings that hinder development and inflate costs, and raise house prices and reduce housing affordability.

6.12 Federal, State and Territory Governments, as a first step, honour their commitment to abolish stamp duties on business conveyances of real property made in the 1999 Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations (which, well over a decade later, has still not been delivered).

6.13 This should be followed by a rigorous review of the impact of stamp duty on residential property, and alternate approaches to revenue-raising.

6.14 The Federal Government in conjunction with the State and Territory Governments, prepare and publish annually a stocktake of the approaches to developer/infrastructure charges used by all State, Territory and Local Governments in Australia.

- 6.15 The stocktake would examine, inter alia, the nature, the processes involved and the incidence of the developer/ infrastructure charges imposed on 'brownfields' and 'greenfields' (both fringe and infill) developments for a normalised set of developments (eg four bedroom, two bathroom detached dwelling; a twelve unit apartment block).
- 6.16 Over time, this work be integrated into the Productivity Commission's annual Report on Government Services (ROGS) processes, to enable existing and prospective home owners, and the residential construction industry, to engage in competitive benchmarking of local governments across the nation.
- 6.17 Federal, State and Territory Governments step up their commitment to deliver substantive outcomes which raise labour productivity growth rates, such as:
- greater flexibility of labour markets, emphasising genuine enterprise bargaining;
 - improve the outcomes from, and returns to, skills education and training, particular in areas of existing and expected skills shortages;
 - reducing the income tax burden borne by wage and salary earners, through further increases in tax thresholds and reductions in marginal tax rates, and the introduction of full tax indexation;
 - reducing the labour taxes imposed on employers, such as payroll tax, as well as broader reform of the business tax system; and,
 - the elimination of inefficient regulations which distort market signals, through regular, rigorous and transparent regulatory impact assessment processes.

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