

# Charter Insight

## The Devil is in the Detail

### The Reality of FIRB Real Estate Data

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The Foreign Investment Review Board (FIRB) is currently considered the most accessible and comprehensive indication of the quantity and origination of international investment into Australian assets.

Foreign investment into real estate assets attracts a disproportionate level of attention, but is perhaps understood the least.

This is the third Insight in a series relating to foreign investment in Australian residential real estate. The previous Insights discuss the relativity of market fundamentals underpinning investment and the impact of currency fluctuations on off-the-plan apartment contracts.

It is important to understand that the prescriptive nature of data tracked by FIRB, as well as its accounting methodology, implies that published FIRB figures will differ from actual realised offshore capital flows. This is especially true for residential real estate.

While the figures and values will differ from actual realised capital flows, FIRB data still serves as a reasonable representation of the broader market narrative.

The most recent FIRB data (FY15) outlines the general state of approved foreign investment into Australian assets. The realities of this data must be properly understood to appreciate the true impact upon the Australian real estate market.

#### NATIONAL FIRB APPROVAL FIGURES

In FY15, there was a record of \$96.9 Bn in approvals for Australian real estate from foreign purchasers (inclusive of residential and commercial assets). By value, 63% of these approvals involved residential real estate (\$60.8 Bn).

Of the residential real estate FIRB approvals, \$28.7 Bn (47% of residential approvals by value) related to Advanced Off-The-Plan (AOTP) approvals, which, as outlined below, overstate the reality of residential real estate capital flows.

#### ADVANCED OFF THE PLAN (AOTP) APPROVALS

AOTP approvals are sought by developers to allow them to sell up to 100% of their project overseas without purchasers requiring individual FIRB approval (the developer essentially receives FIRB approval on their behalf, prior to the sales campaign). However, there are conditions on this sale process.

AOTP approvals can only be granted to developers for permitted projects of 50 or greater dwellings and are limited to \$3M of aggregate sale value per purchaser (in a specific project). The project must also be marketed locally.

Reported AOTP data relates to the total gross potential sale value of all apartments in projects and not the aggregate of actual contracted sales to offshore purchasers. This is important as not all off-the-plan sales from these projects will be to overseas purchasers.

Significantly, AOTP approvals data is not attributed to any individual country and are assessed independently within the FIRB data.

While the value of real estate FIRB approvals attributed to China is significant, it will

understate the reality when considering the likely quantum of dwellings from AOTP projects sold to Chinese purchasers.

#### THE CHINA NARRATIVE

The major discussion point with regards to the FIRB figures has concentrated around the value of approvals to purchasers originating from China. According to FIRB data, approvals originating from China (for both residential and commercial assets) increased from \$2.42 Bn in FY10 to \$24.35 Bn in FY15 with the most significant uplift recorded since FY13 (\$5.93 Bn).

While the current value for FIRB approvals originating from China is significant, it would appear these figures only consider approvals granted to individual purchasers (where purchaser origin is specifically identified) and do not consider the proportion of AOTP approvals directed to purchasers from China. AOTP approval is granted before sales commence and therefore no purchasers are known or origins specifically identified.

#### VICTORIAN FIRB APPROVALS

While the value of approvals in Victoria is high, it is not unexpected given how the off-the-plan market has evolved in Australia (more specifically Melbourne and Sydney).

Of the \$28.7 Bn in FY15 AOTP approvals across Australia, 72% related to projects in Victoria and New South Wales, with Victoria accounting for \$12.85 Bn in AOTP approvals (NSW recorded \$7.77 Bn).

There were AOTP approvals granted for 152 projects through Australia in FY2015 of which 62 projects (41%) were in Victoria.

In FY15, Victoria recorded \$25.58 Bn in total residential real estate FIRB approvals, this compares to \$19.75 Bn recorded across NSW. The primary difference between the two relates to the difference in relative AOTP approvals.

#### STAGING IS IMPORTANT

While these numbers may appear large (especially in reference to their historically modest base), the impacts of increased capital flow and potential settlement risk may not be as simple as it initially appears due to the staged completion of these projects.

It is critical to remember that AOTP approvals, along with aggregate individual approvals, in any single year will have staged settlement over multiple years (typically 2-5 years from the granting of AOTP approval to the developer).



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Projects of significant scale, most notably within Melbourne's Central City Region (CCR) receive FIRB approvals alongside comparatively modest projects, each of which will have significantly different settlement timeframes.

Staging limits the major component of existing market risk to the tranche of projects settling in the existing environment and not the entirety of the portfolio approved by FIRB (or any Authority).

### THE CURRENT CONTEXT

Within the current environment, most FY16 (and similarly FY17) settlements for off-the-plan residential dwellings from international purchasers will originate from FY13 and FY14 FIRB approvals.

These 2013 and 2014 figures will include the individual approvals for new apartments as well as advanced off the plan approvals aggregated.

In total this relates to \$4.2 Bn and \$10.4 Bn (FY13 and FY14, respectively) of FIRB approvals for residential development in Victoria. Of this, AOTP approvals account for a significant proportion (\$6.7 Bn in FY14, FY13 AOTP figure cannot be isolated).

Projects that received recent FIRB approval should not necessarily be considered strictly against the backdrop of current financial and banking conditions.

Recent approvals (FY15) will be delivered over a 3-5 year period due to the distribution of projects to be completed, including those of significantly greater scale, pushing out settlements and capital transfers further into the future for some projects (Figure 1).

### FUTURE DELIVERY OF CURRENT APPROVALS

If we assume the year of a project's launch as a proxy for the period in which FIRB

approval would have been sought for a project, we can better appreciate how the individual FIRB approval years will translate into actual capital flows.

Considering the highest proportion of these projects are likely to be located within Melbourne's CCR (across Victoria), this submarket will be analysed with reference to FIRB approvals to give an idea of how these approvals are incorporated into the market (there is recognition, however, this base is increasingly expanding outside of the CCR).

Charter's proprietary apartment database provides some clarity around the expected completion of these projects and may act as a proxy for the anticipated timing of financing requirements.

According to Charter's database, current FIRB approvals (FY15) are anticipated to be delivered over a 5-year period, commencing in FY17 (Figure 1).

The completions of apartments within the CCR (likely encompassing a component of the FY15 FIRB approvals) will be primarily located within Docklands, in the near term (FY17 and FY18), and delivered predominantly by local developers.

Apartment completions delivered by international developers will commence in FY18 and will be more evenly distributed across Docklands and St Kilda Road. Those delivered through the peak year (FY20) will be highly concentrated across the CBD North and CBD Grid precincts.

Across the CCR, there will be more significant completions and settlements commencing in FY19 (local developers) and FY20 (offshore developers), while FY16 and FY17 are comparatively restrained (Figure 2).

Looking into the future, the majority of FIRB approvals through FY16 are likely to remain

elevated with the greatest component of these completions due in FY19 and FY20.

### THE TAKE AWAY

The recent increase in global Chinese capital investment is an important issue for the Australian real estate market to understand. The FIRB approvals are unprecedented but they are not unexpected given the evolution of the Chinese economy and increased willingness of Chinese capital to invest offshore for multiple reasons, including the greater sophistication of Australian real estate markets and the commoditisation of new apartments as a form of financial instrument for investors.

Although this phenomenon is comparatively recent, it is one that is likely to remain. It should be understood that the quantum of capital flows does not carry risk in itself, but it is how the increased capital flows are managed and staged that is of increasing importance to settlement risk, notwithstanding the broader lending conditions. Current settlements are less exposed to international purchasers (from FIRB approvals) than those anticipated to commence in FY17 and FY18.

### IMPORTANCE OF FIRB DATA

While the data produced by FIRB is the most comprehensive and easily accessible, it also relates only to, and has meaning within, the strict parameters and methodologies applied by FIRB.

It is of increasing importance to look beyond the simple headline figures reported by the FIRB and understand the market context that these figures fit within. The figures in isolation are of little meaning unless they are considered with regards to the functioning and understanding of the broader real estate market within which they exist.

Figure 1: Expected Completion & Settlement Years-FY15 Approvals (FIRB Proxy),

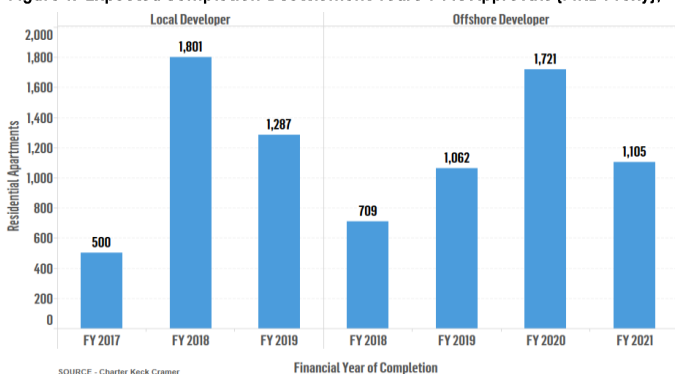
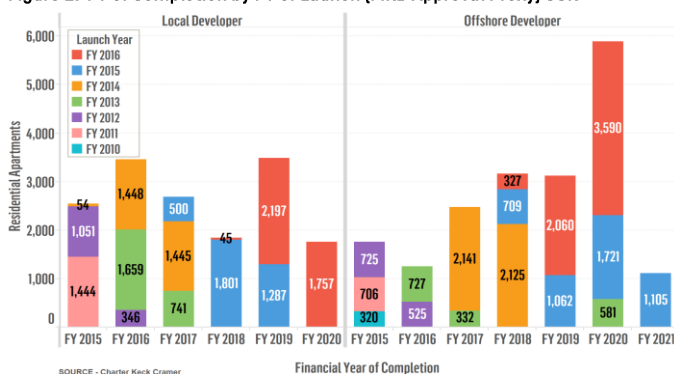


Figure 2: FY of Completion by FY of Launch (FIRB Approval Proxy) CCR



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