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Let’s start tracking hot real estate money

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New Zealand needs to follow Australia’s lead and collect good data on who is buying real estate.

It has become less fashionable these days to look jealously across the Ditch and observe how much better the Aussies are at weather/being rich/having, you know, a real city vibe.

We've been getting more cocky since late 2013, when we were able to say 'nyah, nyah, our economy is growing faster than yours' for the first time since 2006.

However, just because Australians are financially embarrassed doesn't mean all their ideas are useless.

Take residential property investment, for example.

Australians have a reasonable idea how much of their increasingly expensive housing is being bought by overseas investors.

In a report dated May 6, Credit Suisse helpfully crunched the latest numbers from the Foreign Investment Review Board and estimated $A8.7 billion ($9.4b) of housing had been bought by investors or recent migrants from China alone in the last financial year.

That number was equivalent to 15% of new housing supply and was 60% higher than a year earlier, it said.

According to the FIRB's 2014 annual report, China was the largest source of overseas investment in real estate in the previous year, followed by the US and Canada.

In terms of overall overseas investment, real estate was far and away the most popular asset, accounting for $A75b of $A167b in investment approvals granted by the FIRB.

Those are big numbers - and there are lots more where they came from - but it's important to note a couple of things about them.

One is that they exist at all, because New Zealand doesn't have any idea of the equivalent numbers on this side of the Tasman.

The other is that as far as residential property is concerned the overseas investment number is predominantly in new housing stock, because Australia's overseas investment rules are designed to promote development and limit overseas demand for existing houses.

Basically, foreign investors can't generally buy houses that are already built.

Keeping good data

Australia gets full marks for good sense on both counts.

Since the primary function of a house is as a place to live, it makes sense to ensure that people who might actually live in it have first dibs.

Where a house doesn't yet exist, it makes sense to encourage its creation by opening the door to investment.

And if you have a policy like that, it makes sense to have some data to track where the money is going.

Aha, you might say, but the policy has clearly not prevented Sydney's house prices going nuts - and you'd be right. According to the Australian Bureau of Statistics, Sydney's house prices grew 12.2% in the year to December 2014.

Maybe we should have a closer look at that.

An Australian House of Representatives report on foreign investment in housing was published last November. It found that the quality of information on foreign investment was still poor. More seriously, it found "a significant failure of leadership at FIRB, which was unable to provide basic compliance information to the committee about its investigations and enforcement activity."

Enforcement of Australia's rules on foreign ownership of housing appeared virtually non-existent. Not one court action had been taken since 2006 and no divestment order - where a foreigner was required to sell a house owned illegally - had been made during the entire course of the governments of Kevin Rudd and Julia Gillard.

Tighter enforcement

"It defies belief that there has been universal compliance with the foreign investment framework . since 2007," said the report.

It appears large amounts of overseas money have been going into existing houses despite the legal restrictions, hence the government's announcement on May 2 of tighter enforcement and higher penalties for breaking the rules.

This extra demand has the potential to tip the balance of the market. In a game of musical chairs, it's having just one more player than chairs that creates the tension.

New Zealand, where there are no restrictions on foreign investment in housing, must be an increasingly attractive target. As Credit Suisse said: "Perhaps the Chinese buyer will consider Auckland more closely given zero government charges."

Criminal investment

We also must take account of criminal investment. By its nature we can't be sure how much is washed through the real estate market, but way back in 2004 it was estimated that $A651 million of criminal funds was invested in Australian real estate annually - the figure was quoted in a submission to a 2014 parliamentary committee inquiry into financial crime.

According to the Australian Transaction Reports and Analysis Centre: "Australia-based and overseas-based crime groups use professionals such as lawyers, accountants, financial advisers and real estate agents to help undertake transactions."

Lawyers who think that payments made through a bank account are automatically clean are hopelessly naïve.

Ron Pol, a lawyer working on a PhD about the investment of criminal funds in New Zealand real estate, has a wealth of information about the extent of the danger.

Let's remember too that this money may be derived from or used in particularly nasty activities such as terrorism, sex trafficking and illegal arms trading, as well as plain old theft, corruption and extortion.

It looks to me as if we have at least two good reasons to collect proper data on who is buying real estate. What's the holdup?