What does the 2017-18 Australian Federal Budget mean for the AREIT sector?

MAY 2017

Canberra targets the residential sector with the Budget posing limited direct implications for commercial real estate

Even before it was delivered, almost all the Nation's most influential economic commentators expected the 2017-18 Federal Budget to be loaded with policy positions addressing housing affordability, foreign investment and negative gearing. They certainly weren't disappointed.

In what has been labelled "a Labour budget handed down by a Liberal government", the 2017-18 edition was heavy on initiatives aimed at alleviating stresses within the residential markets of the country's two largest capital cities. Proposals to assist first home buyers as they save a deposit to simply enter the market, foreign buyer volume restrictions, supply growth initiatives and some minor tweaks to negative gearing were some of the standouts.

Let's look at some key proposals geared towards the residential property sector:

- From July 1, savers will be able to salary sacrifice extra contributions into their superannuation account above the compulsory contribution, up to a maximum of $30,000 in total and $15,000 in a single year. They will then be able to withdraw that cash from July 1, 2018 onwards, along with any associated earnings, for potential contributions towards a house deposit;
- New developments will be subject to a 50% cap on foreign investment approvals to "safeguard the opportunity for Australian buyers to purchase". "We will restore the requirement that prevents developers from selling more than 50% of new developments to foreign investor," the Treasurer said. The new rule applies only to developments with at least 50 units. The current level is 100% after the Rudd government lifted it from 50%.
- A range of measures announced in the Budget include working with States and Territories to reform planning and zoning laws, releasing surplus Commonwealth land for development, and establishing a $1 billion National Housing Infrastructure Facility to "address infrastructure chokepoints that are impeding housing development in critical areas of undersupply".
- Negative gearing remains, but rules are being tightened around what can be claimed, specifically depreciation deductions and travel expenses.
- From July 1, 2018, people aged 65 and over will be able to make a non-concessional contribution of up to $300,000 from the sale of their principal residence into their superannuation, provided they have lived in their residence for at least 10 years.

We actively manage our portfolios away from the riskier earnings, including those from residential development, preferring the stability of commercial property rents instead. Our exposure to residential property in the APN AREIT Fund is less than 10%.

Cognisant of this focus, we note the following potential impacts of the latest Budget on the domestic commercial real estate market:

- The Bank Levy may result in increased interest rates which will have a two-fold impact on the AREIT sector generally – potentially higher debt costs, lower consumer discretionary spending and possibly slower broader economic growth;
- The Bank Levy may result in lower deposit rates, which might see a further swing to passive, relatively low risk income focused investments like commercial property;
- Restrictions on residential investment noted above might potentially make commercial property investing more attractive, increasing product demand;
- Ability to increase personal contributions to super from downsizing may also provide more support for income focused investments like commercial property.

As we have highlighted above, the 2017-18 Federal Budget initiatives as they relate to the national real estate sector has concentrated on addressing concerns within the residential market. We will continue to monitor the proposed Budgetary measures as they are enacted but see little direct implications for the commercial real estate market at this stage.

APN Property Group
A specialist real estate investment manager

We actively invest in, develop and manage real estate and real estate securities on behalf of institutional and retail investors. APN's approach to real estate investment is based on a 'property for income' philosophy.

Established in 1996, APN's listed on the ASX and manages $2.4 billion (as at 31 December 2016) of real estate and real estate securities. APN trades on the ASX under the code 'APD'.

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