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EXECUTIVE SUMMARY

- Australia continues to receive solid foreign investment interest as shown by the in excess of 11,000 proposed transactions approved in 2017–18, representing a combined potential investment value of $163.1 billion.

- In 2017-18, there were nevertheless declines in approvals by both number and proposed investment value for both residential and non-residential sectors. The value of approvals for the manufacturing, electricity and gas sector decreased 59.3 per cent, while the value of approvals for the services sector increased 11.8 per cent. Such large shifts are not unusual as proposed investment in a sector in a particular year may be elevated by high-value or competing proposals. Proposed investment in a sector is also impacted year-to-year by factors such as the state of the sector and sale offerings. In residential real estate, there was a decline in New South Wales' share of approvals, which was offset by increases in Victoria and Western Australia's shares. The decrease in residential real estate approvals by value was driven by a drop in new dwelling related approvals. Like other similar economies we have seen a decline in proposed investment from China as Chinese authorities have tightened capital controls.

- A total of 1,024 business applications worth $150.6 billion were approved in 2017–18. These figures are down from 2016–17, with 125 fewer approvals and around $17 billion less of proposed approved investment. A large portion of the decline by value in comparison to the last two financial years is attributable to a drop in the number of large proposed transactions (over $2 billion), which aligns with a decrease in sales of major energy and infrastructure assets. The last two financial years were also elevated by competing foreign bids for such major assets – the proposed foreign investment approvals data covers foreign investment approvals, not actual foreign investment, so double counting occurs when multiple investors bid for the same target.

- For the first time since 2012–13, the United States surpassed China as the largest source country for approved proposed investment due to an increase in United States approvals and a decline in Chinese approvals. The United States recorded an increase in approved investment from $26.5 billion in 2016-17 to $36.5 billion in 2017-18, with significant increases in real estate and the manufacturing, electricity and gas sector.

- China was the second largest source country following a decrease in approved proposed investment to $23.7 billion in 2017–18 from $38.9 billion in 2016–17. This reduction was due to falls in the value of approvals across all sectors. Over the last five years, Chinese proposed investment peaked at $47.3 billion in 2015–16 and also reached $46.6 billion in 2014–15. While proposed investment will not necessarily translate to actual investment and such datasets are not comparable, International Monetary Fund and Australian Bureau of Statistics data to the end of 2017 indicate that Australia has been impacted to a lesser degree by the decrease in Chinese outward investment compared to similar economies.

- In 2017–18, there was a significant increase in proposed investment approvals in service sectors, particularly in health care and the finance and insurance sector. With increased investment in these areas, protection of personal data and data security continued to be an area of focus for the Board and other agencies, such as the Critical Infrastructure Centre (CIC).

- By number of approvals, 91 per cent were for proposed investment in residential real estate worth $12.5 billion by value. This was a drop of $17.5 billion from 2016–17 reflecting a slowing in foreign demand for residential real estate.

  – The main driver of the drop by value was a decline in new dwelling related approvals, in particular, in developers seeking exemption certificates that provide pre-approval for foreign persons to purchase new dwellings in developments. However, approvals in the same category were significantly elevated in 2014-15 and 2015-16 at three to four times the average of the immediate years prior.

  – Consistent with the overarching principle of Australia's Foreign Investment Policy that proposed investment in residential real estate should increase Australia's housing stock, 84 per cent of approvals by number were for categories, such as new dwellings and vacant land for development, that contribute to increasing Australia's housing stock.

  – While Chinese demand for residential real estate has fallen, China still accounts for a majority of residential real estate approvals.

- Strengthening the foreign investment compliance framework is a key area of focus. In 2017-18, Treasury completed 11 business investment audits relating to more than $25 billion of proposed investment and there was a generally high level of compliance among those audited. The Australian Taxation Office (ATO) completed around 1,400 residential real estate investigations and found 600 properties that were in breach. In most circumstances, an infringement notice was applied to these breaches. The Australian National Audit Office also completed a comprehensive performance review into the management of foreign investment compliance obligations for residential real estate. The final report was largely positive about the processes implemented by the ATO to manage compliance and additional improvements are being made as a result of the report.

- With major reforms having been made to foreign investment regimes overseas, such as in the United States and the United Kingdom, the Australian Government has enhanced its cooperation with counterpart agencies overseas, particularly in relation to national security developments. The comparatively well-developed nature of the Australian foreign investment review mechanism has been the subject of close scrutiny by other like-minded countries as part of their consideration of addressing national security and other issues relevant to their foreign investment regimes.

OVERVIEW OF REPORT

This report has four chapters and four appendices:

- Chapter one provides an overview of the Foreign Investment Review Board (the Board) and the Foreign Investment Review Board (FIRB) agencies,[1] including responsibilities, membership and operational costs;

- Chapter two discusses the accomplishments and challenges faced by the Board and FIRB agencies in 2017–18. It reviews the changes to the foreign investment framework, stakeholder engagement conducted by the Board and FIRB agencies and the redesign of the FIRB Application Portal;

- Chapter three analyses data on foreign investment applications finalised in 2017–18. It includes approvals data by number, value, sector, and investor country. It also includes data on variations and foreign investment application fee collections;

- Chapter four explains key developments in Australia's foreign investment framework compliance program. It discusses the approach to compliance by FIRB agencies, and the work underway to strengthen assurance that foreign persons are meeting their obligations. This includes stakeholder engagement and education, audits and investigations, and the imposition of penalties under the *Foreign Acquisitions and Takeovers Act 1975*;

- Appendix A lists Board members' attendance at Board meetings;

- Appendix B provides an overview of the main methodological and data caveats that apply to applications and approvals data in this report. Of particular note in this regard is the transition, in 2017–18, from identifying the source country of proposed investment based on who controlled or likely controlled the investor, to the ultimate known underlying ownership of the investor;

- Appendix C sets out the examination and approval process for foreign investment applications; and

- Appendix D contains a glossary.

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1 The Board is supported in its responsibilities by Treasury's Foreign Investment Division and Public Groups and International in the Australian Taxation Office (ATO). Treasury and the ATO are collectively referred to in this report as 'FIRB agencies'.