

THE **COMPLETE BEGINNERS**  
STEP-BY-STEP GUIDE TO

# bankable residential property development

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**S**o you want to become a property developer? Well, you're in for quite the adventure! Ask anyone in the property development/finance industry who has a decade or two's worth of experience about the leading indicators of when the property development market is getting overheated, and they will likely highlight a sharp increase in the number of first time/amateur/inexperienced speculators/investors/developers entering the market who are competing for development sites with the experienced campaigners.

Unfortunately, what happens next is sharp rise in prices being paid for land, an equally rapid fall in the profit margins – and therefore a heightened risk is being taken on by individuals with the least amount of experience to make site work on such fine margins of error. What happens next? A flood of additional supply at heightened prices; construction prices go up; buyers start running out; incentives start coming into the market; projects become unviable and have to be sold down in an overinflated market at the wrong end of the property cycle. Sites fail to sell, mortgagee sales are on the rise, the inexperienced developers are wiped out and the experienced developers start acquiring again – and around we go again.

The natural process described above has been seen time and time again, which is the reason why financiers are particularly cautious of first time or relatively inexperienced property developers.

This paper is obviously not meant to be an exhaustive guide to property development; however, it does serve to highlight some of the key considerations for first-time property developers to ensure you don't get caught in the above scenario.

By far the most important acknowledgement you need to make is that *you simply don't know what you don't know*. By acknowledging this simple yet vitally important truth you are already a long way to greatly reducing your risk and thereby greatly improving your chances of making your first project less stressful and more profitable.

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You are then able to recognise how essential it is to surround yourself with a team of highly experienced advisors to guide, mentor and protect you from the many pitfalls and risks associated with property development.

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- The key team members you need are:
1. A specialist property finance advisor
  2. A town planner
  3. A development manager
  4. A property solicitor.
- this product appeals to a very thin part of the market and discounts many of the purchasers I mentioned above.
- In this market, your potential buyers include first home buyers, investors, SMSF's, downsizers and the bulk of the owner occupiers.
- The important elements of this product are:

4. A property solicitor.

By following the steps outlined below you will greatly reduce the various risks associated with property development and optimise your profits.

The importance and value of being able to confidently sell your stock quickly into the deepest market (which is affordable and high yielding) through multiple sales channels is hard to overstate for a number of very good reasons.

**STEP ONE:** \_\_\_\_\_ **STEP TWO:** \_\_\_\_\_

*Start where they are always the most number of buyers*

There is always a higher number of potential buyers in the affordable and high yielding end of the residential property market.

*Design your product with the buyers in mind*

Now that we have established which market to focus on, the process of designing your product becomes easier. Every specific element of the design of the product you

market. Every specific element of the design of the product you are developing must support your product being able to developed at affordable price point for owner occupiers and generate the highest possible rental returns whilst still maintaining an acceptable level of quality.

You should develop in only major metropolitan locations. I will describe more about the importance of the location of the properties you should consider developing in the balance of this paper.

The affordable product types you should focus on developing include house and land packages, town houses, units/apartments and duplexes. Developing vacant land lots as an entry level developer is not recommended as

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### STEP THREE:

*Do your research and paper trade first*

It is vitally important you start with a hypothetical feasibility and cash flow first before you go looking for a potential site to purchase. Yes, that's correct – you heard me right!

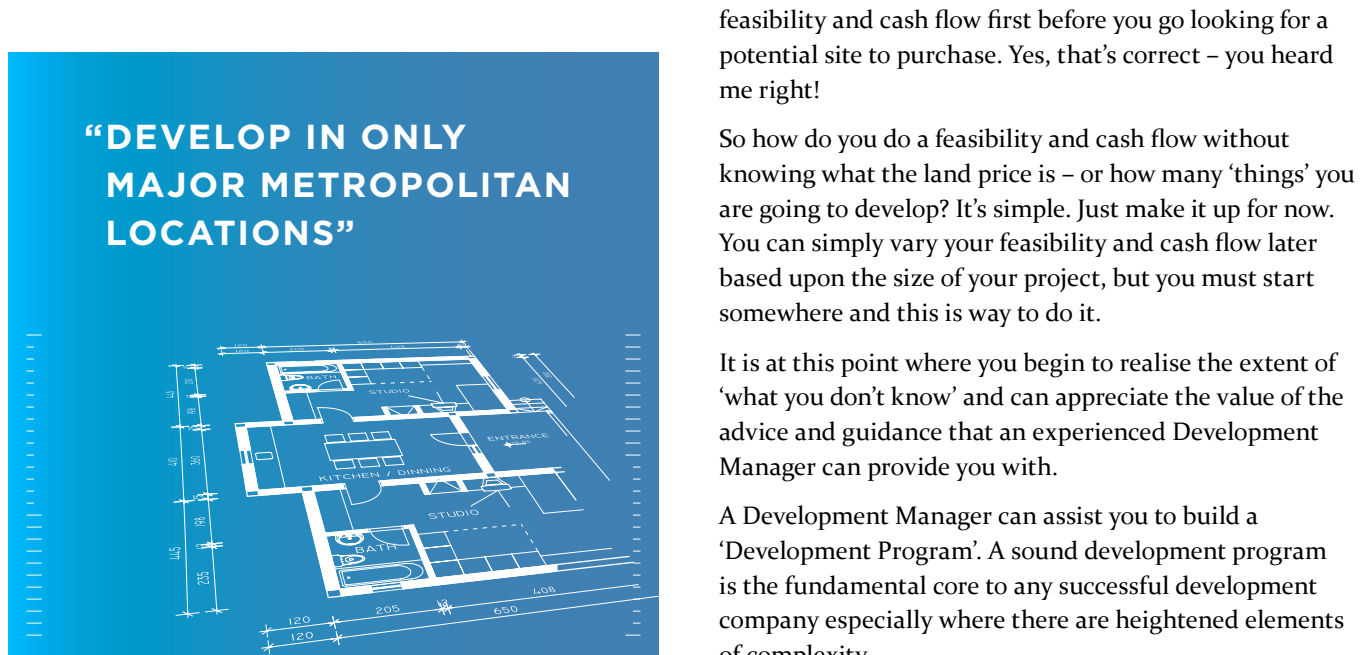
me right!

So how do you do a feasibility and cash flow without knowing what the land price is – or how many ‘things’ you are going to develop? It’s simple. Just make it up for now. You can simply vary your feasibility and cash flow later based upon the size of your project, but you must start somewhere and this is way to do it.

It is at this point where you begin to realise the extent of 'what you don't know' and can appreciate the value of the advice and guidance that an experienced Development Manager can provide you with.

Manager can provide you with.

A Development Manager can assist you to build a 'Development Program'. A sound development program is the fundamental core to any successful development company especially where there are heightened elements of complexity.



The development program (DP) is built by your Development Manager (DM) based on what is the highest and best use of the site. The DP consolidates and reconciles the overall development cashflow, development milestones, development feasibility (staged and consolidated) and investment returns over time.

The DP co-ordinates all of the five key individual strategies outlined below into a real time single reporting and planning tool:

1. Design, Approvals and Community Consultation
2. Valuation
3. Marketing, Advertising and Sales
4. Structured Finance – Debt and Equity
5. Delivery – Project Management & Construction

It is essential all of the future consultants in the project control team led by the DM are ultimately accountable to the DP. The DP forms also forms the basis of what is reported against on an actuals-to-budget basis to all key stakeholders.

The DM generally prepares what is called a desktop report.

The desktop report provides a critical path and overall business plan to move a project forward based upon a staged set of priorities which is properly cash flowed and resourced.

The completion of a desktop report often forms part of the DM's initial staged scope of works and it is the DM's responsibility to assist you to profitably turn the vision of the project into a reality.

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### STEP FOUR:

#### *Get valuation support and QS Support*

For the development program to be valuable, it must be evidence-, valuation- and QS-based and supported. Through obtaining valuer and QS support the key assumptions of your feasibility and cashflow become more bankable in future, which greatly reduces your financing risks later.

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### STEP FIVE

#### *How will you finance the Development Program?*

It is obviously at this point that you should be working closely with your financial advisor/property banker to understand how you are going to finance the entirety of the DP from beginning to end relative to personal financial capacity.

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### STEP SIX:

#### *Find a specific site*

So after having completed the steps you are better prepared to go to market to look for an appropriate site to develop. By this stage you will have a good understanding of what development sites are worth based on what the zoning of the land is likely to yield in term of the number of units.

There are many ways in which to locate a potential site to develop, both off-market and advertised. Regardless of which way you go about potential site acquisition, your acquisition activities will be far more focused and efficient having completed the steps above.

## **“AS AN ENTRY LEVEL DEVELOPER YOU SHOULD NEVER CONTRACT A SITE WITHOUT A DUE DILIGENCE CLAUSE”**

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### STEP SEVEN:

#### *Secure the site under Due Diligence*

As an entry level developer you should never contract a site without a Due Diligence clause giving you sufficient time to properly investigate the specific risks of developing the site.

At this point, a suitably experienced solicitor can greatly reduce your risk by ensuring your purchase contract is set up in such a way so as to reduce the development risks in line with your development program.

The primary risk at this point is the Development Approval (DA) associated with the land if the site does not already have a DA. If the site does not have a DA it is essential you, or your DM, engage a town planner to advise you of the DA risk of the site and what is the potential number of units that can be developed on the site.

Once the DA risk is understood, your DM will be able to assist you in overlaying your hypothetical DP to this site. Specific heritage, ecological, environmental, traffic, easements and other legal searches should also be completed.

It is essential that your financial advisor/property banker has provided you with a conditional finance approval prior to you going unconditional

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### STEP EIGHT:

#### *Co-ordinate design, approvals, valuation, QS, CMS, presale contracts, finance approvals and marketing*

It is essential that you and your DM co-ordinate the design and approval consultants, advertising and sales agents, solicitor, valuer, bankers, builder and project manager to efficiently realise the project milestones within the preconstruction phase of the DP in order to prepare for the land settlement.

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### STEP NINE:

#### *Obtain DA, settle the land*

Having obtained the DA, it is essential you do all things necessary to provide the Valuer with the necessary information to value the land for mortgage and construction purposes. The investment you make in the process can make a vast difference in the as-is valuation you get back from the Valuer – which can greatly affect the equity you hold in the site and the overall financing costs and profitability of your project.

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### STEP TEN:

#### *Launch the marketing program*

Having completed the previous steps, you are now well prepared to enter into the sales and marketing and

construction-letting phase of the development program.

The selection of a highly experienced and successful marketing and sales agent is one of the most important steps in the process and can make or break the success of the project.

There are many consideration when it comes to the overall marketing program including:

- Number of presales required by the bank
- Sales schedule needs to be within 5% of the project valuation
- Sales rate required to met the milestones contained with you Development Program
- Overall cost of marketing and sales commissions
- Quality of your sales being defined by the mix of investors, locals, owner occupiers and overseas purchases
- Strategic stock releases to different buyer groups.

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### STEP ELEVEN:

#### *Preparation and tender of the construction contract*

A construction contract provides the framework by which construction will progress on the project. It effectively outlines the deliverables and apportions the delivery responsibility and risk for these works. According to David Hume of Highgate Management, “It is very important to match the appropriate form of delivery (type of construction contract) to the key outcomes that the developer is trying to achieve”.

Key issues to consider for the preparation and tender of the Construction Contract will include:

- The developer’s project objectives
  - Risk profile of the developer and its capacity to carry risk
  - The financier and or equity partner’s requirements
  - Financial capacity of developer
  - The size of the project
  - The quality of development
  - The location of the development
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- The type of development (i.e. residential, industrial, commercial)
- The size and capability of the builder
- The likely response of the builder to the form of contract put forward
- Sales contract deliverables
- Titling deliverables
- Statutory requirements.

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### STEP TWELVE:

#### *Delivery, titling and settlement*

This is the point of the project where it's essential to have everything in place so that settlements are achieved efficiently and effectively. Interest on your borrowings is going out the door at its most rapid pace, as you will be likely to be getting close to fully drawing down your construction facility. It is also your opportunity to save as much as possible in interest costs by ensuring you reach settlements as quickly as possible.

Optimising the outcome requires that you proactively manage the development from the start. However, at a certain point in time – well before construction works are due to reach completion – the development and construction team needs to be focussed on what we call the 'construction completion phase' of the development to ensure that your pre-sales will settle as efficiently as possible.

Depending on what state you are in will depend on the terminology used, however the key issues and deliverables at this stage of the development are essentially the same.

Pre-lodgement processes are available and can help mitigate unforeseen issues and reduce times for final reviews and endorsements by statutory authorities.

Key considerations include:

- Development consent includes the appropriate titling required (this can be a separate or additional approval to the consent to undertake works on the site)
- Construction works are completed
- Development consent conditions are satisfied



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- Builders defect completion program
- Construction certificate (or BA/Ops works or Building permit conditions – depending which state you are in) are satisfied
- Any easements required for the project are registered as early on as possible
- Any caveats or other encumbrances are dealt with
- All fees and contributions are paid (depending on what type of development it is and what state you are constructing the development in largely dictates timing for payment of developer contributions)
- Titling surveys are achieved as early as possible in the construction process
- Community management statements are finalised and in place
- Body corporate insurance is in place
- Body corporate (owners corporation) has been created



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## WHITE PAPER

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- Developer insurance is in place on unsold development stock
- Deliverables under sales contract have been satisfied and co-ordinated
- Notice to purchasers has been provided in accordance with the sales contract
- Communications with purchasers – it is important you manage your purchasers so that there is no surprises and they all have funds ready and in place so that they can settle at the earliest date possible
- Pre-settlement inspections need to be co-ordinated
- Bank valuations on behalf of purchasers need to be co-ordinated
- Any refinance facility that may be required is in place.

Out of absolute need the team at DFP have developed an end-to-end inhouse advisory service to guide and support first-time and relatively experienced property developers through the twelve steps mentioned above.

Any member of the DFP team would be delighted to speak with you more about how we may help. ●

**MATTHEW ROYAL** has extensive experience in the property development and investment industry, with exceptional knowledge and understanding of the financial criteria and methodology used in assessing property development and investment proposals. Prior to co-founding DFP, Matthew was an Associate Director of Property Finance QLD with Bankwest Business, facilitating mortgage structures up to \$100 million. Over the past 10 years Matthew has also held executive and non-executive directorships in numerous private and public companies.



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