How To Fund Your Development In A Changing Financial Environment

The Urban Developer

HALL CHADWICK
Chartered Accountants and Business Advisors

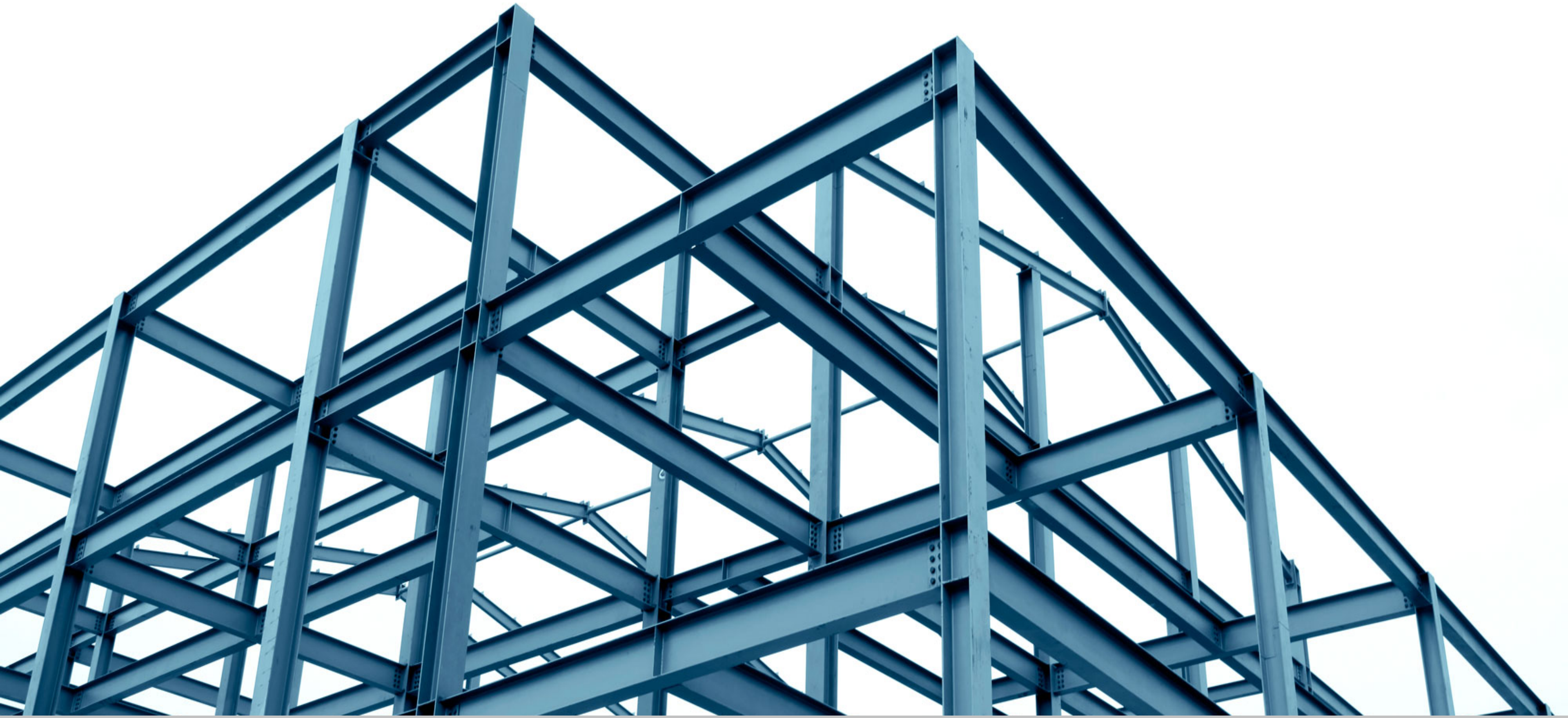
DFP
Development Finance Partners

WELCOME

Adam Di Marco

Founder & Publisher

The Urban Developer



Findings from the recent Urban Developer Survey

Current Trends and Sentiment

The Urban Developer

HALL CHADWICK
Chartered Accountants and Business Advisors

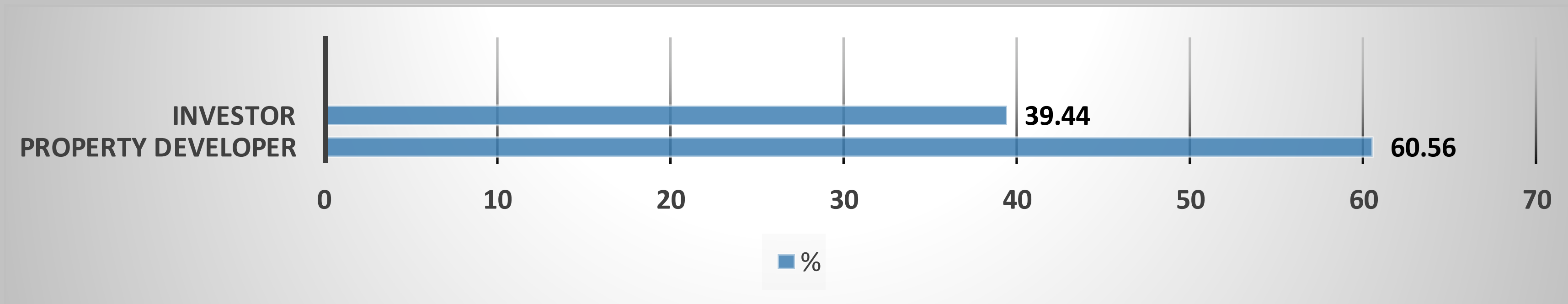
Development Finance Partners

About The Survey

180 **respondents**

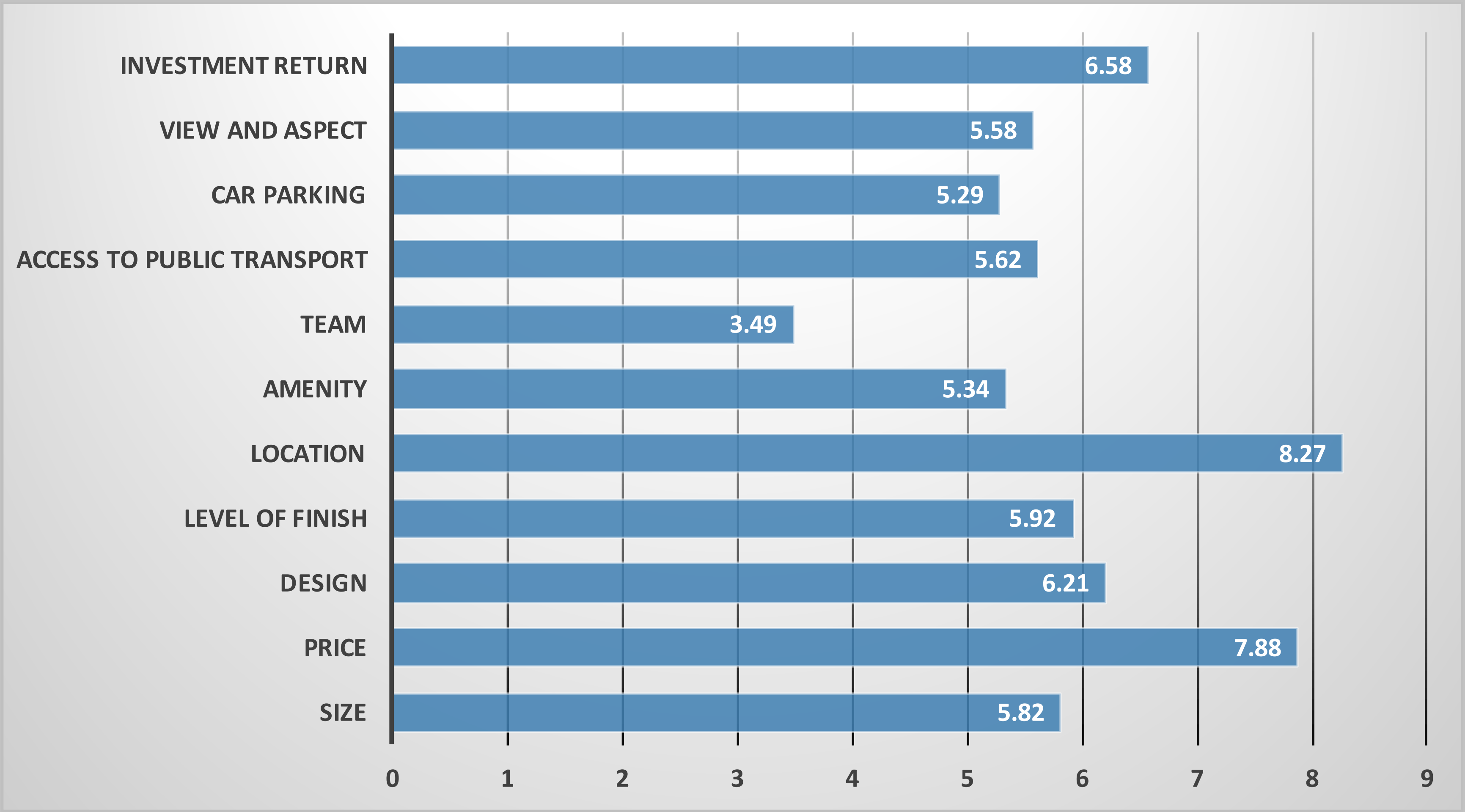
National

Are You a Property Developer or Investor?



Answer Choices	Responses	
Private Company (< $5m / year turnover)	42.78%	77
Private Company ($5m - $20m / year turnover)	16.11%	29
Private Company ($20m - $50m / year turnover)	5.00%	9
Private Company ($50m+ / year turnover)	10.00%	18
Public Company	7.22%	13
Other (please specify)	18.89%	34
Total		180

Rank The Importance of The Following Buyers' Preferences

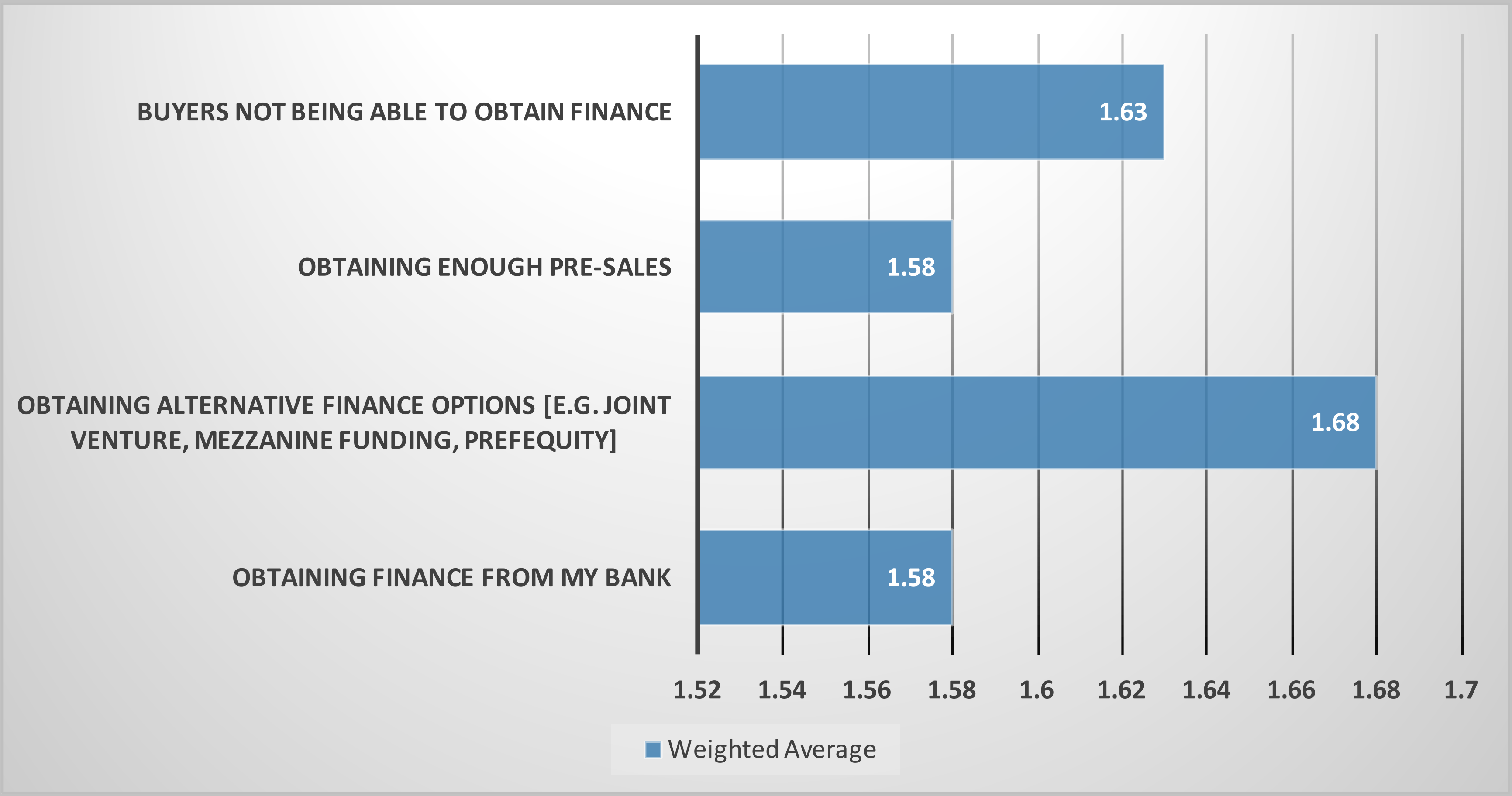


The Urban Developer

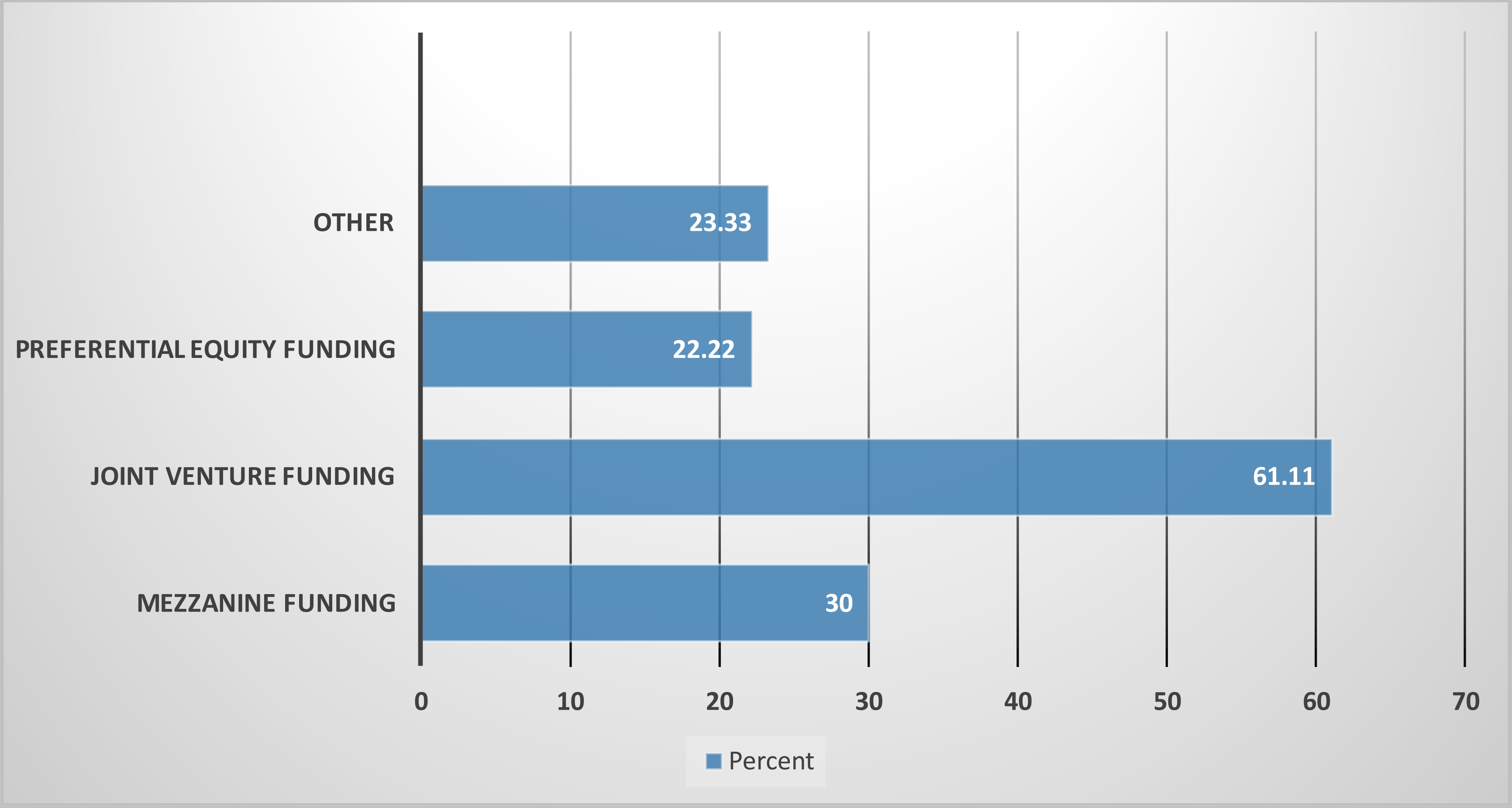
HALL CHADWICK
Chartered Accountants and Business Advisors

DFP Development Finance Partners

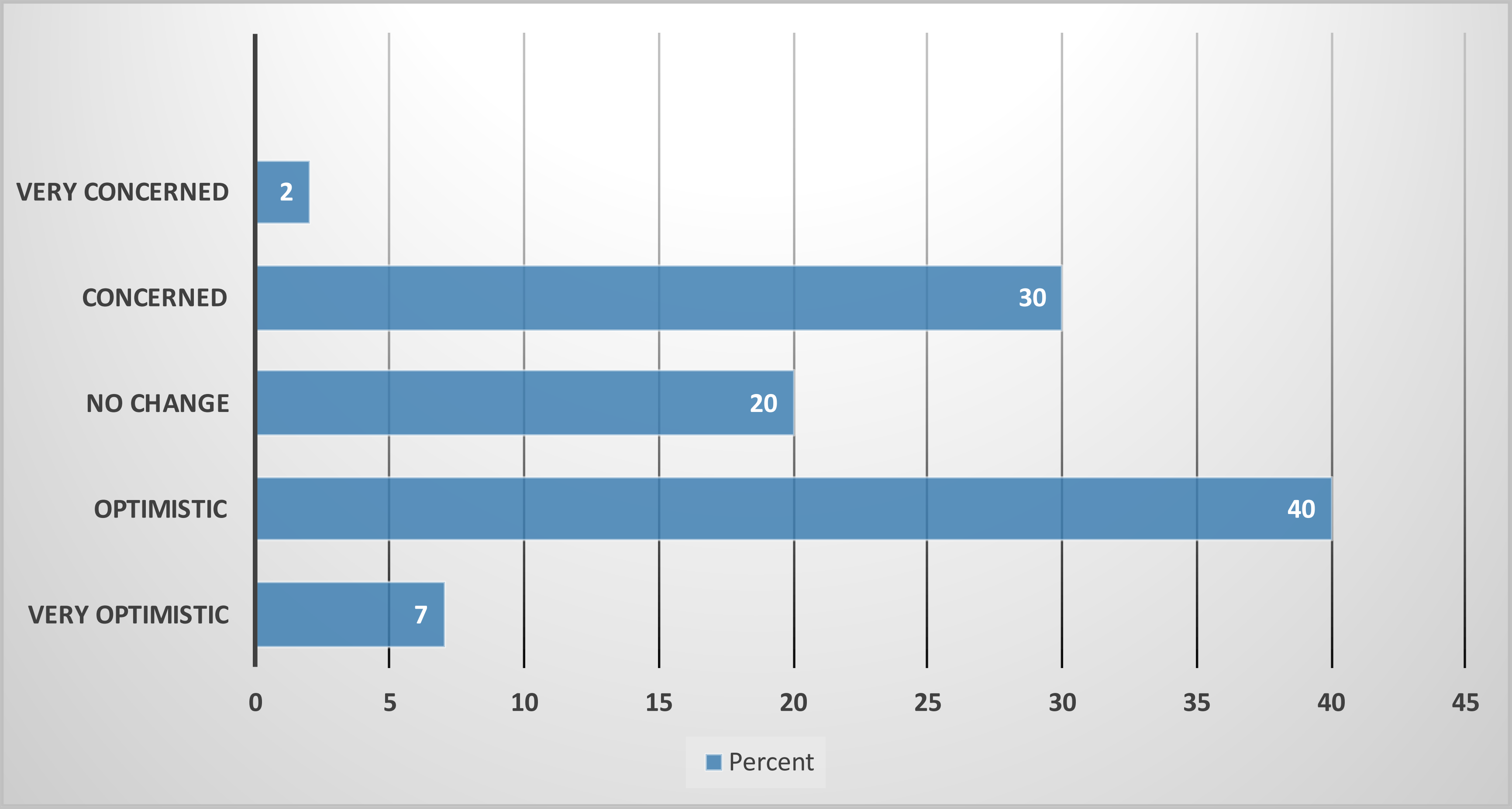
What Are The Biggest Finance-Related Issues Affecting You At The Moment?



In the last year, have you investigated any of these non-bank alternative finance for your developments?



How do you feel about the outlook for the next 12 months compared to the previous 12 months?

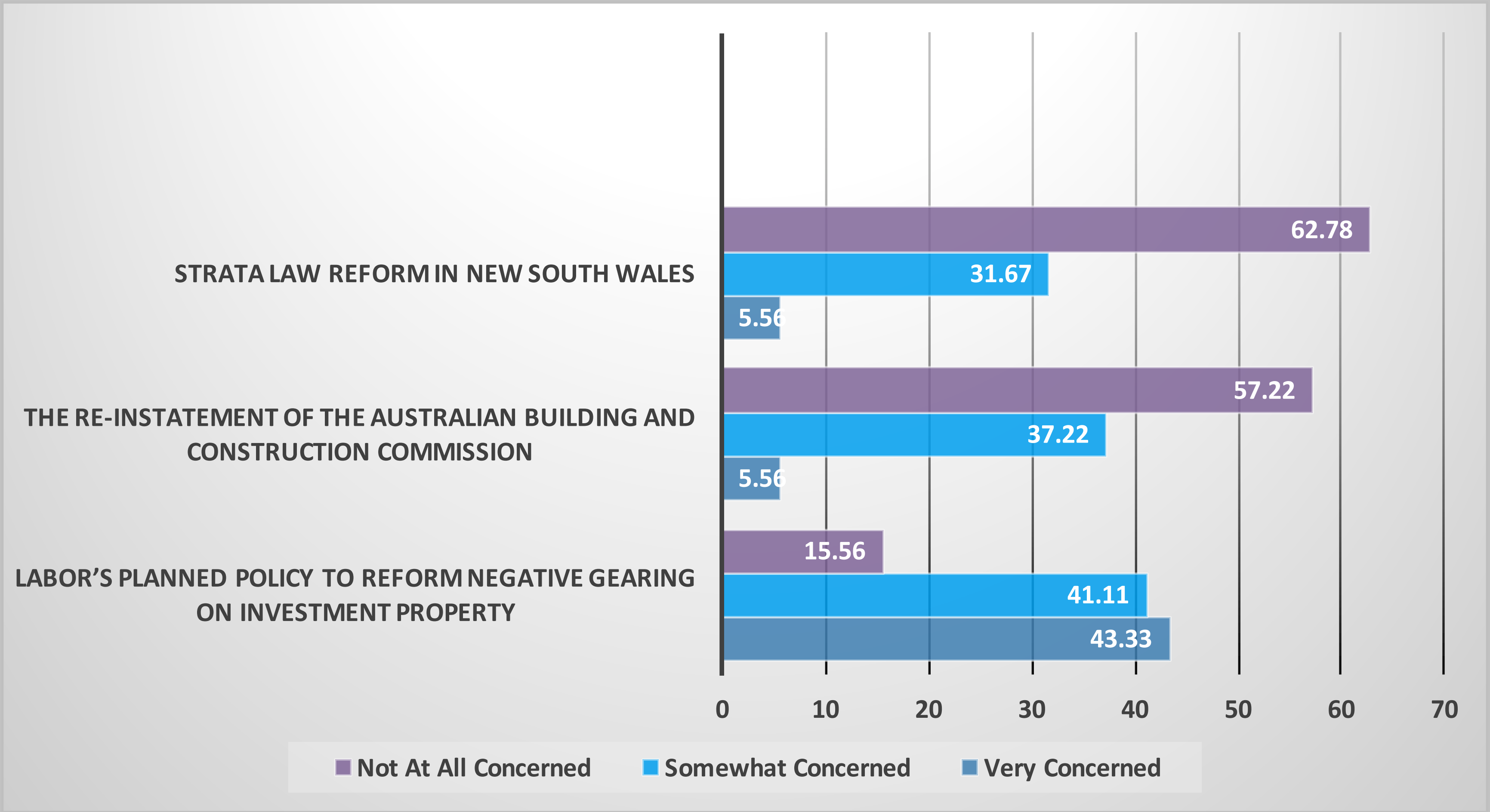


The Urban Developer

HALL CHADWICK
Chartered Accountants and Business Advisors

DFP Development Finance Partners

How concerned are you about the following potential political changes?



What you should be doing now

De-risking and Gearing For Success

The Urban Developer

HALL CHADWICK
Chartered Accountants and Business Advisors

DFP Development Finance Partners

Top Down Approach

- Global Macro
- National Macro
- Industry Fundamentals
- Sector Segmentation Fundamentals
- Sponsor Risk
- Project Risk

Key Local and Industry Macro Factors

- Population growth
- Economic activity
- Real wealth
- Credit growth
- Employment
- Housing completions vs Demand vs Supply
- Long term interest rates

De-risking: Sponsor and Project

RISK GRADING RATING 1 - 10

Project:

		1			2			3			4			5			6			7
RG	W	LOCATION	RG	W	SPONSOR	RG	W	SALES RISK	RG	W	COMPETITION	RG	W	PROFIT & RISK	RG	W	GEARING	RG	W	EXIT
		Amenity			Liquidity			Competition			Builder			Profit Margin			On Comp			Financing Risk
		Transport			Experience			Size			Design Risk			ROE			TDCR			Fund Through Take Out
		Employment			Value of Guarantee			Presales			Construction Contract			Term			Residual LVR			Valuation Risk
		Education			Credit History			Quality of Sales			Basement			Settlement Risk			Debt Cover			QS Risk
		Affordability			Reputation			Total Sales Budget			LD's						Sensitivity			
		Supply Existing			Character			Local Market Appeal			Prelet %						As Is LVR			
		Population Growth			Builder			Existing Stock			Fixed Price Term									
		New Supply			Sponsors Cash			New Supply												
		Rental Yield						Depth of Market												
		Mortgage Approvals						Price Point												
		Investor / Owner Occupier						Point of Difference												
		Depth of Market						Quality												
		Competition						Value for Money												
								Rental Yield												
								Owner Occupier												
								Downsizer												

De-Risking Presentation

Who is the applicant?

What is being developed?

What is the loan amount?

Market risk

Loan to value ratios

Make up of project equity

Project feasibility

Capability of the builder

Borrower's & guarantor's financial capacity, experience and reputation

Delivery risk – applicant and builder's experience

Security offered

Quality of the sales

Exit strategies

Project location

Potential profitability of the applicant

Funding Structure

Product	Bank	Non Bank	Non Bank >6M	Mezz
Interest Rates	BBSY + 2% + 1.5% Line = 6% pa	9.75%	11%-16%	15%-20%
Fees	0.35%-1%	1%-2%	1%-2%	2%-4%
LVR	70%-75% TDC	80% TDC	80% TDC	85%-90%
	50%-60% On Comp	65% On Comp	65% On Comp	75%-80% On Comp
	40% on Land Only	65% on Land Only	65% on Land Only	75% on Land Only
Presales	100-130%	0%-30%	50%	80%-100%

Turning plans into reality

Case Studies

The Urban Developer

HALL CHADWICK

Chartered Accountants and Business Advisors

DFP Development Finance Partners

Scenario 1

- Client required us to finance the acquisition of the land via company share sale agreement and finance the construction costs associated the development of thirty eight (38) residential apartments located in Chermside Qld.

Financing Challenges

DFP were retained to provide advice and recommendations on the following:

- Developers had no development experience.
- Acquisition of the site had to be settled via a share sale agreement.
- Developers price list was well below market rates.
- Valuation came in significantly lower than land purchase price.
- No presales at land settlement.
- Client has insufficient equity to finance the development.
- Local apartment in oversupply.
- Builder was forced to renegotiate construction contract due to cost escalation.

Results

DFP's recommendations were adopted by the client and DFP were retained to implement those recommendations which has resulted in the following outcomes:

- DFP raised the required capital to settle the share agreement which effectively settled the Land.
- DFP negotiated a vendor finance facility with the Vender of the Land.
- DFP advised, arranged and settled a construction finance from Retail Bank on favourable terms.
- DFP advised, arranged and settled a mezzanine finance facility.
- DFP negotiated a significant reduction to the Builders Construction Cost Escalation based upon unconditional finance offers.
- DFP advised upon a 5% increase in the sale prices of the 38 apartments.
- 25 Apartments were achieved on the increased sales
- Construction is underway.

DFP Funding Table

Funding Table	Soft Equity	Cash Equity	Purchase	Vendor Finance	Mezzanine	Senior	Total
Land	-$550,000	$1,225,000	$2,750,000	$550,000	$975,000	$0	$2,200,000
Land transaction costs	$78,572			$0	$0	$0	$78,572
Construction Costs	$0	$602,000		$0	$485,000	$7,613,000	$8,700,000
Consultant & PM fees	$0			$0	$0	$405,448	$405,448
Statutory fees	$0			$0	$0	$978,218	$978,218
Project contingency	$0			$0	$0	$435,000	$435,000
Land Holding Costs	$0			$0	$0	$38,000	$38,000
Miscellaneous	$0	$329,865		$0	$0	$287,421	$617,286
Finance charges	$0			$0	$174,000	$152,400	$326,400
Interest	$0				$610,000	$353,842	$963,842
TOTAL COSTS	**-$471,428**	**$2,156,865**		**$550,000**	**$2,244,000**	**$10,263,329**	**$14,742,766**

Summary of financial results achieved:

- Senior Debt: 60% of GRV and 73% of TDC
- Mezz: 73% GRV and 85% TDC
- Vendor Finance: 90% of TDC
- Development Profit Margin - 22% at Land Value

  - 11% at Land Cost net of all costs

- $2,200,000 net project profit vs forecasted loss of $750,000
- Return on Investment 115%

Scenario 2

- Client requested DFP to advise and arrange Joint Venture Capital to deliver three (3) medium density residential projects located in Melbourne VIC.

Financing Challenges

DFP were retained to provide advice and provide recommendations based upon following financing challenges:

- All three sites did not have a Development Approval
- Client was unable to offer any real property security offered
- No Senior Debt Finance Approvals had been secured
- Owner Builder
- Gearing to 100% of TDC

Proposal

1. DFP advised Steller Projects that an unsecured loan note guaranteed at the parent company level was preferable to a Joint Venture Facility.

Results

- DFP's recommendations were adopted by the client and DFP were retained to implement those recommendations which has resulted in the following outcomes:
- DFP arranged a corporate loan note facility to finance the initial three (3) projects plus additional funding finance an additional eighteen (18) projects with a combined GRV of circa $800,000,000.
- Minimum client IRR achieved across all projects was 100%.
- Steller Projects maintained full control of their business and projects.

Why effective structuring is important in a tightening market

Structuring

The Urban Developer

HALL CHADWICK

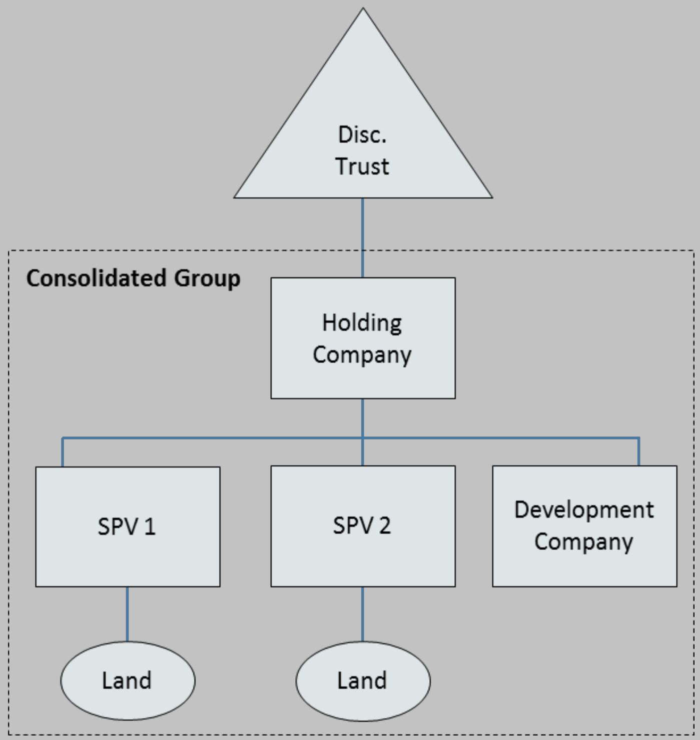
Chartered Accountants and Business Advisors

D F P

Development Finance Partners

Develop and Sell: Tax Structuring for Multiple Simultaneous Developments

Consolidated Group with Special Purpose Vehicles

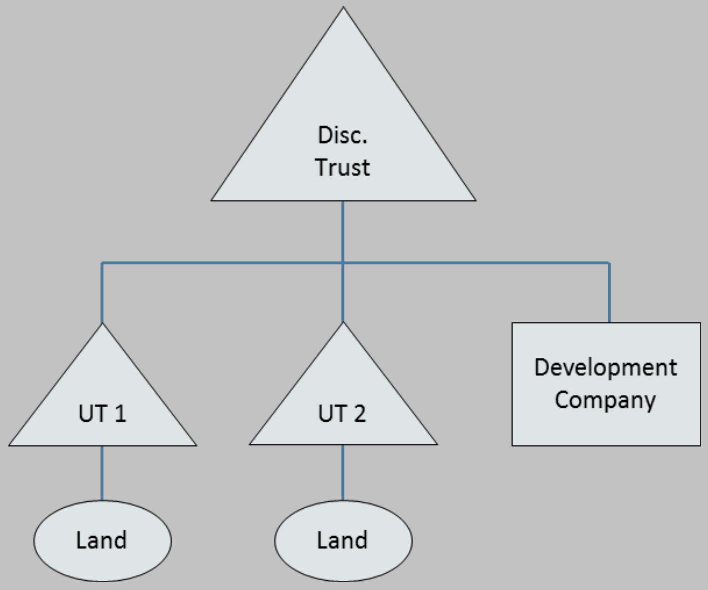


Benefits of Structure

- Ability to get true value for group equity.
- Flexibility.
- Asset protection (stakeholders and entities).
- **Ability to offset losses / expenses in one entity against those in another entity.**
- Avoids "management fees" and ATO problems.

Develop and Hold:
Tax Structuring for Multiple Developments

Develop and Hold Structure

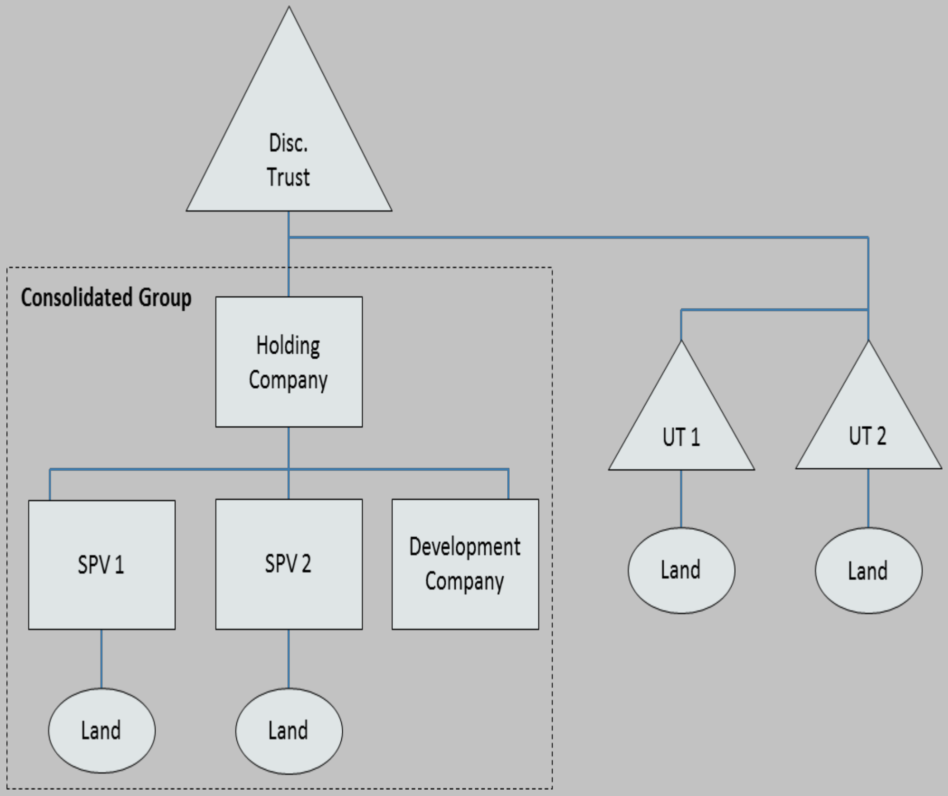


Benefits of Structure

- Flexibility.
- Asset Protection.
- Individual beneficiaries of Discretionary trust can access 50% CGT discount on sale.
- If implemented correctly avoids mistakes in negative gearing.

Develop and Hold Some and Sell Other: Combined Structure

Develop and Hold Some and Sell Other Structure



Benefits of Structure

- Partitioning (keep the penthouse)
- Reduces GST if implemented correctly
- Reduces stamp duty

Development Companies and the Importance of Development Agreements

Availability of a Deduction for Expenses

- Costs of Development
  - Net basis
  - Gross basis
  - Trading stock
  - Holding costs
- Development company will allow the developer to get a deduction for the expenses immediately.
- If development company is a member of a consolidated group, this results in significant timing benefits

Contrast with methodology that sees expenses included in value of trading stock for assessment on a net basis

State Tax Issues Update

Land Tax Liability During Development of Rural Land used for Primary Production

- No land tax will be payable if relevant land is used for predominantly for primary production.
- The NSW OSR seeking to assess farmers for land tax on properties that will be developed.
- The court in Metricon Qld Pty Limited held in favour of the taxpayer and ruled that the predominant use of the land is determined by reference to physical use of the land, not economic potential.
- No land tax is payable where the relevant land is an operative farm
- This is a significant win for the taxpayer.

Stamp Duty for Foreign Purchasers

- Various states are starting to introduce a higher level of stamp duty for foreign purchasers – e.g. Victoria.
- The additional duty rate is 7%.
- This is a significant economic disincentive for foreign purchasers of Australian property and should be considered in light of a developer's sales strategy.

Final Thoughts

- Foreign buyers
- Secrecy
- Thin cap
- Assets in the wrong structure
- Selling piece meal to super

Contact me at dkenney@hallchadwick.com.au

Q&A

The Urban Developer

HALL CHADWICK

Chartered Accountants and Business Advisors

D F P

Development Finance Partners

Thank You

/TheUrbanDeveloper

/TheUrbDev

The Urban Developer

The Urban Developer

HALL CHADWICK
Chartered Accountants and Business Advisors

DFP
Development Finance Partners