Fact sheet

Property development finance

Borrowing for property development is generally considered speculative by lenders, so obtaining finance can be difficult unless you have significant experience, with a good track record and substantial capital backing. It is highly recommended you work closely with a mortgage adviser experienced in this area to obtain a successful finance application.

Residential lending

- Small developments up to three or four units may qualify for residential lending, which is significantly cheaper in terms of rates and fees and less complex to apply for.
- Generally, your application will need to show: income verification and rental potential to prove you can service the loan, 20% deposit (there is typically an 80% LVR), building plans, council approval and builder insurance.
- The loan will often be similar to a land and construction loan, where qualifying is partially based on income from the units being rented out rather than pre-sale requirements.

Commercial lending

A development bigger than three or four units may qualify for a commercial loan. In this case lenders are usually much more conservative than for residential loans, commercial development loans have a different structure and features, and accessing finance is more expensive and requires significantly more paperwork.

The loan:

- LVR: usually up to around 70% of the cost of the project and lenders may also require the security of another property.
- Interest rates: typically higher and may include a risk margin depending on the size and scale of the project.
- Fee structure: you may be charged a percentage of the loan amount (between 0.5% and 1.5% depending on the strength of your application).

The application:

It is crucial to understand how banks will assess your application and this is where an experienced mortgage adviser is essential in assisting you to put it together.

On top of your financial situation and capacity to repay the loan, lenders will assess the following:

- Your experience (including details of past projects and profit made).
- Builder's reputation (details of past projects).
- Current project details (building plans, DA approval, building contract).

Top Tips

- Start small and build up your experience in property development before considering a large property development.
- Developments smaller than three or four units may qualify for residential lending, which is much simpler and cheaper.
- Lenders require a huge amount of detail in applications for commercial property development finance and expect a high level of professionalism.
- Commercial lending attracts higher rates and fees, may incur an added risk margin, and typically has a lower LVR.
- Development finance is a complicated process and it is highly recommended you work with an experienced mortgage adviser who knows what lenders require.

Need help?

Everyone's circumstances and requirements are different. Speak to your Smartline Adviser to discuss your commercial finance needs.

This sheet provides general information only and is correct as at the document date (28/11/2018). Please refer to your Smartline Adviser for full details.

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- Viability of the project through each stage (current value of the property, end value of the dwellings compared to median price of dwellings in area, site description, size of units, zoning, capital growth and population growth in the area, design concept, experience of your development team, projected sales figures and profit, timelines, proof of budgetary and cash controls, feasibility study with allowance for contingencies).
- Evidence of presales if on-selling, or a promising rental market analysis if planning to retain ownership (this may require you to have a larger percentage of equity).
- Fire-sale price of the property.
- The professionalism of your finance application.

Experience:

You will need a successful track record in smaller projects before lenders will consider financing a larger development. It is recommended you start with a single dwelling renovation or duplex, then progress to small developments of three to four units before you take on a larger development. This also allows you to build the skills you need such as budgeting and dealing with builders and banks.

Good to know:

- You may be able to borrow the ongoing interest as part of your finance package – so you don't pay interest during the construction phase. However, the interest is capitalised (i.e., you will pay interest on the interest the following month) and you can't go above the LVR.
- You may want to consider different types of lending for the various stages of the project such as:
  - an acquisition or development loan to cover purchase, development application and pre-construction costs
  - a construction loan to cover the building costs
  - an investment loan if you are keeping the property as a long-term investment.