LeadDeveloper

Improve Your Game With Development Economics

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How Easily Development Economics Can Improve Your Development Game?

Property Development Economics

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How Can Property Development Economics Improve Your Development Game?

Developers who are looking to cut expenses and increase profits should consider how property development economics can help them. A 'cost reducing' mindset is usually prevalent in awful real estate developments, but a more cost-effective & cost saving approach would be beneficial for all parties involved with the process!

Successful property developers take a calculated approach to cost-cutting. They encourage their design team to look at the structure's finances without losing the concept and atmosphere to help the real estate development sell.

Understanding the essentials of real estate economics can help you save money in the long run. Traditionally, a developer client will request sketch blueprints from an architect.

The design team's brief is to develop a practical structure that will appeal to both renters and buyers, pleasing appearance while also considering the project's economics. The architect and the rest of the design team should be reminded that capital invested in the design phase of a property development project is lost if there is no return on investment. Good design may be more expensive, but the benefits will surpass the expense if applied wisely.

In this article, we discuss the economics of site selection, architectural design, alternative construction methods, and outline the most evident difficulties that the developer should consider when the contractor's tender price is too high. So, let's dive in.

What Is The Property Development Economics?

Development economics is the process of leading a property development team to create a development that is aesthetically beautiful, functional, and cost-effective and whose value grows over time. The application of the real estate economics process is ongoing and should be followed from the beginning to the end of the project.

The project's success is dependent on the sum of the decisions taken during this procedure. Each action, such as swapping out one part for another, must contribute to creating a product that will sell or lease well and perform well for many years.

The development economics process begins with a project's initial concept or idea and the site's pre-purchase feasibility and continues during construction and long after the contractor has left the site. The developer must be adaptable and resourceful throughout the process to discover solutions to each new difficulty, no matter how big or small it is. Based on every piece of cost data gathered throughout the process, the developer will make assumptions.

Excellent property development economics aims to keep the number of assumptions to a minimum. By removing these assumptions, the developers will be more confident in completing the project on time and within budget.

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With a solid understanding of real estate economics or property development economics, the developer should enlist the help of all property development team members by explicitly stating the project's goals and objectives. All too often, development team members pursue their wishes and objectives for the project. This needs to be avoided from the start.

As the key decision-maker, the real estate developer and each team member must realise that meeting the project's goals and ensuring that it is viable and delivering the anticipated return is critical to its success. If this return is not achieved, the project will be unable to be funded, and development will cease.

How Does Location Affect The Property Value?

A property developer's top objective is to find a development site in the ideal location, but this is only one consideration; there may be physical cost constraints beyond the developer's control that make the site untenable. Any of the following could be one of them.

The Site's Shape

A rectangular or square site is significantly more cost-effective than an irregular one.

Slope

The higher the slope, the more expensive it is to construct. Because foundations and supporting structures are more complicated, this is the case. Excavation and the requirement for retaining walls are increasing, and drainage difficulties are becoming more prevalent. The area of external walls grows as buildings descend a slope.

Plot Proportion

When determining the price of a site for sale, a real estate developer should consider the rate per square metre for the raw

land and the cost per plot ratio for the entire building(s) and the cost per unit for residential developments. For example, if $3 million is requested for a 1200 square metre site zoned with a plot ratio of 2.0, the following rates can be calculated:

- Price of raw land: $3000000/1000 = $3000 per square meter
- Price of plot ratio: $3000000/2000 = $1500 per Square meter

The State Of The Soil

To support a structure, poor foundations may necessitate further engineering. Sandy or clay soils may require deep concrete piles to achieve sufficient support.

Take a look at the below table to compare different soil types and conditions.

Comparing Typical Development Site Soil Types And Conditions

Class	Foundation
A	Most sand and rock sites, with little or no ground movement from water changes
S	Slightly reactive clay sites, with only slight ground movement from moisture changes
M	Moderately reactive clay or silt sites that can experience moderate ground movement from moisture changes
H	Highly reactive clay sites that can experience high ground movement from moisture changes
E	Extremely reactive sites that can eperience extreme ground movement from moisture changes
P	Sites that include soft soild, such as soft clay or silt or loose sands, landslips, mine subsistence, collapsing soils, soils subject to erosion, reactive sites subject to abnormal moisture conditions or sites that cannot be classified otherwise

Other Factors In Development Economics Related To Site

The following are some more factors that may influence the cost of a site during the selection process.

Access

Material handling becomes more complex and time-consuming due to poor access. Isolated sites, such as those only accessible by water, drastically raise the costs of supplies and labour.

The Site Is Being Demolished And Cleared

Demolition and site clearance can account for up to 10% of the cost of a new structure in some situations. Contamination issues, such as asbestos removal can considerably increase the cost of construction.

Excavation

Excavation is time-consuming and expensive, and it frequently necessitates shoring up or underpinning surrounding foundations. The expense of rock excavation can be pretty high, especially when drainage concerns arise.

Service Accessibility

Getting services like water, electricity, sewerage, drainage systems, and gas are challenging in specific remote locations.

Remote provision of these services is costly. Distance from mains can also be a concern in less isolated regions.

How Does The Design Affect The Building Cost?

When we examine two buildings that have been planned to suit the exact needs in terms of floor space, we often find that one costs $1500 per square meter and the other costs $1000 per square meter. Further investigation reveals that they share the same external and internal finishes and comparable roof and floor structures. There appears to be no reason why the rates should not be the same, but it does happen.

A real estate developer and the design team should assess the cost implications of various planning and architectural aspects at the design stage of the property development process. Several design elements can cause cost overruns, but if the developer and team grasp the principles, they can help keep costs in check.

The Layout Of The Plan

The cost of a structure is heavily influenced by its layout—the more straightforward the layout, the lower the cost.

Plan Form

Even though we may strive for a basic plan layout, the plan form may cost differently.

Wet Areas And Interior Walls

The quantity of internal walls and moist regions is another aspect that affects construction costs. Kitchens, bathrooms, laundries, and toilets have a higher cost per square metre than dry areas. The rent per square metre for a building of one-bedroom flats will range significantly from the rate for a block of three-bedroom apartments.

The Ratio Of The Perimeter To The Floor Area

A plan shape directly impacts the exterior boundary walls. The perimeter to floor area ratio helps us analyse several plans to determine the most cost-effective solution: the lower the ratio, the more cost-effective the proposal.

It's important to remember that the perimeter cost might be as much as 20% to 30% of the entire cost and that an external wall is twice as expensive as an internal partition. It would be best to consider other design elements, but the perimeter to floor area ratio allows a more experienced developer to determine the best ratio as part of the design criteria in the architect's brief.

Unoccupied Spaces

Corridors, entry halls, tunnels, stairs, and lift lobbies are considered dead spaces that you cannot use productively, yet they still require air conditioning, lighting, cleaning, and maintenance. Minimising these spaces during the design phase thus has a clear financial benefit. When calculating the cost of

dead space, the practical and aesthetic values must also be considered; nonetheless, diligent evaluation can result in significant savings.

Amalgamating Services

Bathrooms, kitchens, and laundries (wet areas) located near or above each other in high-rise buildings such as apartment blocks can reduce the cost of supplying services by avoiding extensive runs of concealed plumbing and piping. Similarly, combining many utilities in a single trench or conduit duct might save money.

Other Design Considerations In Property Development Economics

Other factors that could affect the design's cost include:

Floor to ceiling height: Extending the height of the walls increases the rate per square metre.

Building height: Comparing unit rates for single-story and multi-story buildings reveals significant variances. Scaffolding and the number of contractors working at higher levels have increased as multi-story structures have grown.

Constructional distinctions: There is a significant reduction in cost if prefabricated concrete walls are used. Or if industrialised building methods are used instead of traditional ones.

Finish and architectural detail variations: The standard of finishes necessary, particularly on vertical components of a building, should be carefully considered.

Standard measurements: Standard dimensions are available in many building materials and fabricated components, such as aluminium windows and doors. With designing in mind, you

can reduce cutting and waste. Custom sizes are always more expensive than standard sizes.

How Does Construction Methods Affect The Real Estate Development Cost?

Construction is the area that receives the most attention when cost savings are sought, even though, as previously said, other elements can have a considerable impact on development costs.

Many creative brains in the construction business have invented many walling techniques. However, walls are only one component of a structure, including flooring, roofing, kitchen layouts, and other elements. The developer and design team should evaluate all aspects of construction cost savings rather than focusing on just one.

Below you will find several approaches that can be used, but before choosing a building system, keep the following points in mind.

Traditional Methods Vs. Low-Cost Building Systems

Traditional methods are the cheapest and most acceptable building approach, depending on the area and type of development, because the skills and resources are readily available. On the other hand, low-cost building techniques that limit the consumption of materials and cut construction time can save a lot of money. On the other hand, some newer products have yet to stand the test of time.

Materials With A Low Cost

Low-cost materials often appear cheap; nevertheless, their appearance can be improved by the way they are subdivided, detailed, and finished. Using low-cost materials where they are not apparent or their performance is not crucial is a practical approach to save money.

A variety of less expensive building materials is also available, but the developer must guarantee that these materials comply with local requirements and the State Building Code.

City Vs Regional Areas

Because of the increased cost of labour and transportation of building materials, building rates in cities are lower than in regional locations for traditional construction methods such as brick and concrete. Prefabricated systems or modular structures in regional locations are less expensive than local, regional rates. Still, when prefabricated or modular competes with traditional construction in the city, there are no meaningful cost savings unless the design is repeated and the product has a critical mass.

Regional areas don't have a lot of options, especially when it comes to price, but can the city's market accept these alternative construction methods?

Prefabrication

Building items in a factory is always faster and less expensive than building on the job site. This is because shelter, materials, specialised machinery, and labour are not always readily available on site.

Only the foundations are built traditionally, while portions of walls, floors, and roof are pre-assembled in a factory, transported to the site, lifted into place by a crane, and bolted together. Prefabricated construction is a building process used to bring structures up faster and more affordably.

Prefabrication can take many forms, from individual components to fully prefabricated homes. Prefabrication shortens the construction process and lowers the project's overall cost.

Modular Volumetric Construction

Volumetric modular construction is a methodology that has been tested for more than 30 years, is constantly evolving, and is quickly becoming the world's preferred building approach. Building components are built at a factory to create a finished three-dimensional room or space, then delivered to the job site and quickly connected to sewer outlets and power sources.

The advantages of factory-manufactured, pre-assembled building modules are similar to those seen in the automobile sector. Onsite construction has drawbacks such as exposure to bad weather and community disruption due to traffic congestion and noise. Prefabricated modular buildings are

becoming more popular, especially for hotel rooms, flats, workplaces, student housing, and schools.

Pods For Bathrooms And Kitchens

Bathroom and kitchen pods use similar volumetric modular building concepts; however, they're only for kitchens and bathrooms. The benefit of this construction process is that while the main structural parts are being erected on site, the pods are being manufactured in a factory. These are installed once the majority of the onsite construction is complete.

Due to the quantity of work conducted in small floor areas, bathrooms and kitchens are the two most expensive parts in a structure and fetch the highest rates per square metre. Completing wet spaces such as bathrooms and kitchens is the most common cause of delays in construction projects. Due to delays, pod construction might save money on interest.

Flat-Pack Systems

All of the building materials are stored at a factory or warehouse. The building components are then carried to the job site in a container as flat packs and erected on site. In the residential construction sector, the flat-pack building technology is often known as a 'knock-down construction' or a 'kit home.' Unlike volumetric modular or pods, the flat-pack system is a two-dimensional system that requires a team of tradesmen to install onsite.

Flat-pack systems save money on freight because they don't have to transport any 'air'. The flat-pack may be less expensive in

terms of proximity, distance, and trade availability, but a comparison of the various products is required.

The Advantages Of Prefabricated, Modular, And Flat-Pack Systems In Terms Of Cost

The following summarises several advantages of employing prefabricated, modular, pod, or flat-pack structures. This category of construction methods is also known as OSM (off-site manufacturing).

Construction Speed

This guarantees a faster return on investment. Off-site construction allows for the construction of the building and the site work to be accomplished simultaneously. It cuts the overall completion time by up to 50%.

Indoor Industrial Construction

Assembly is weather-independent, increasing work productivity and preventing material degradation.

Favourable Pricing

Manufacturers can effectively haggle with suppliers for material savings when they have many similar components. Additional cost reductions come from shorter building times and less reliance on onsite expert labour.

Improved Quality Control

Building modules are finished in a factory setting, ensuring better quality control. Fewer defects or call-backs also improve production efficiencies and dependability.

Minimum Wastage

By repeating the identical plans, it is possible to keep track of accurate material quantities. Onsite construction produces considerable waste that needs removal, but off-site construction produces less waste.

Environmentally Friendly Building

Off-site construction produces less trash, uses less energy and creates less site disruption than site-built structures.

Safety

Buildings constructed in factories have proven safer than traditional construction methods because fewer components are involved.

Self-Supporting

Most prefabricated construction components, formwork, shuttering, and scaffolding are unnecessary.

How Does The Influence Of Contractors Affect The Property Cost?

Because construction costs vary greatly, you must account for site location in your feasibility assessment. Furthermore, due to limitations imposed on the contractor, tendered construction rates may differ within the same town or city. Construction rates are also affected by market factors. Many builders remain competitive during recessions, but rates rise dramatically during booms due to a shortage of tradespeople.

The building contractor you choose can impact the final cost of the project. It is well understood within the construction industry that a builder is only as good as the craftsmen he hires.

Quality and workmanship will degrade due to a low-cost builder's use of low-cost artisans. Before awarding the builder the contract to build your project, it is critical to conduct cautious and extensive due diligence on them. The type of contract you have with the builder is also essential. Costs will be better controlled if fewer loose ends in the contract. In addition, the following factors may impact the cost of construction.

Recommended Reading - 13 Steps Real Estate Market Analysis

Tenders

Although one should set tender arrangements during the sketch design stage, other factors such as market

competitiveness and the quality of tender documents play a part in determining a project's final pricing.

The lowest tender proposed does not always imply that it is the best. If the lowest and second-lowest bidders or other tenders have a significant disparity, ask the lowest tenderer to double-check their figures.

If a builder forgets to include a crucial piece or underestimates the cost, he will try to make the difference elsewhere or face bankruptcy. This might pose many issues because you'd have to locate a new builder to finish the job.

If you discover that the lowest tenderer omitted an item on purpose and then seeks to renegotiate the price, you should avoid dealing with them since they have demonstrated that they are unethical and someone you would not want to work with.

Date Of Completion

You can save money on interest if you finish your project early. Ensure to evaluate the tender price against the construction period, which you might be asked in the tender documents. You may have to accept a higher construction price if a structure is required to be completed in a shorter time than would be reasonably expected and if fines are imposed for any delays.

The higher tender may be the most cost-effective after building time, early trading, and escalation savings are factored in. Although most bids include a penalty for late completion, nearly none include an incentive bonus for early completion.

Variations

After the contract is signed, ensure to keep the variations or revisions to the design to a bare minimum. Builders, like any other business, want to maximise their earnings. They may have won your contract by being the cheapest tender with the smallest profit margin, but they may try to make up for it by charging excessive charges for any adjustments.

If you can't reduce the variants, make sure you and the builder agree on a formula for calculating the cost of changes before signing the contract, such as actual cost plus a fixed percentage.

You might need the property feasibility suite to know your numbers in your development journey.

Contracts

Ensure the contract price is set and contains items finalised before the contract is signed. The same goes for 'cost plus' contracts: make sure there's a system in place to keep the 'cost' under control.

The fundamental to any construction contract is that the price must be steady, with checks and balances in place to account for any possible deviations.

Advance Payments

Ascertain that the progress payments meet the requirements of the builder, the bank, and your financial resources. Because of

their requirement for financial flow, most builders will want frequent payments.

On the other hand, you and your bank will want to make sure that the builder is not paid more than the worth of the work that has been completed on the job site.

If the builder requests a deposit or other upfront payment during the construction process, do not pay unless specified in the contract and negotiated or explained before signing it.

The Impact Of Financing On The Cost Of Property Development

Banks want to make as much money as possible for their investors. The policies and practices of lending institutions vary greatly. Some lenders would not even consider a proposal acceptable to a different lender. A developer's success will be determined by his understanding of various lending institutions' policies, methods, and procedures and the many financing options accessible. Ignorance of these issues can cost money and damage a project's profitability.

Enrol for quick start property development course to understand the development methods.

With so many credit institutions vying for business, the developer should shop around for the most important financial deal. If a loan is approved by the finest two or three institutions, the developer should evaluate each loan offer. Because each institution is unique, examine the terms and circumstances of each offer to see which one best meets the project's requirements. Take into account the following factors that may impact the cost of your project.

Rates Of Interest

Interest rates differ between banks, and even the slightest difference might affect a project's profitability, especially if the construction time is long and drawn out. A rate decrease may be considered if a developer is a good customer with a strong

track record. What if the developer is working with a different lender? In that instance, it is a good idea to spend money upfront on a well-documented project presentation.

Bank Charges

The word "bank charge" refers to all fees and levies imposed on its customers. Many banks charge small fees for services such as requesting a deposit slip or a counter check, as well as notarising a document. Bank fees account for a significant component of bank revenue. These fees can take a variety of forms, including:

- Fees for applying for a loan
- Fees for appraisals
- Mortgage insurance
- Legal representation fees

Check the price of each of these charges and, if possible, try to negotiate a lower price.

Fees For Financial Brokerage

Using a finance broker to secure development money for your project might be advantageous since they can locate lenders interested in the type of project being developed. They will also know which lender offers the best rates, fees, and conditions. However, check the broker's fees before hiring them, which may include the following:

Mandate fee: Some brokers will not begin working until legally appointed.

Monthly retainer cost: Some may require this price, but it is not suggested unless they offer continuing or corporate guidance.

Success/brokerage fee: These fees can range from 2.5 to 5% for seed and equity funding and 0.5 to 1% for debt, but make sure the lender does not cover them.

Authorities' Influence On Development Costs

It should become a habit for a developer to review all fees covered throughout the early phases of the property development process as part of their site due diligence.

The following is a list of possible costs imposed by local governments and other government agencies. Each jurisdiction has its own set of fees, so it's essential to determine which agencies have authority over the development site and what fees will be assessed.

Contributions To Development

The word "headworks" comes from the old method of diverting water at the beginning of an irrigation network and positioning these procedures at the "head of the works." Increased growth pressures and the maintenance of infrastructure standards in the community necessitate the imposition of headworks levies.

Contributions to Headworks are a one-time fee for providing water and wastewater services to your development. These contributions, also known as standard infrastructure contributions (SICs), are GST-free and payable for works on a property up to the connection point, increasing the potential demand for existing water, wastewater, or drainage systems.

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Fees For Submissions

Examples are payments to the local council for development approval and fees to the state government if the development site is amalgamated or subdivided. Building licence fees are usually included in the builder's contract price, and they are paid directly through their builder's registration number/licence.

Fees For Additional Approvals

Other fees may be levied by government authorities in addition to the fees already listed, so verify with your local council's planning department and your development team. Additional charges may include:

- Fees for city inspections

- Electrical power
- The state planning commission
- Fees for estate fence
- Destruction costs
- Council maintenance.

When Plans Go Over Budget

While we have discussed the fundamentals of property development economics with the above points, there will always be cases when the most fabulous planning is not enough to avoid a catastrophe.

Suppose you discover that the overall construction cost has exceeded the budget set in your **feasibility study** after completing the project design and paperwork and the final quotes from the builders arrive. So, what exactly do you do? Do you put the project on hold, or do you and your team go over the plans again and search for other ways to save costs?

What I experienced in my property development journey is not all tenders received are within 100% of the budget; some are 10% above or below the stated value, while others are far more than planned. As a result, if the prices are out of your pricing range, you and your development team must examine every design component for possible suggestions. These suggestions will be re-priced and provided for feedback. The entire development team will then weigh in on the consequences of each decision. Here are some cost-cutting suggestions.

Reducing The Number Of Site Works Is A Good Idea

Changing the elevations to minimise rock excavation or lifting the building to avoid cut and fill reduces expenditures. It may also be beneficial to reroute highways to avoid excavation. Another potential option is to downgrade the quality of roadway and drainage design and reroute them to save plumbing. There are some other ways too:

- Revising the balance of cut and fill calculations is another something to consider.
- Minimising the number of retaining walls and relying on natural banking and drainage systems.
- Lowering the number of paved areas.
- Preserving as many natural areas as feasible.
- Situating buildings for the shortest distance between service connections .
- Leveraging the land's natural contours.

Exterior Construction Of The Building

The building contractor can help lower the construction budget by recommending alternate materials that look comparable but are less expensive. Take a look at the following as well:

- One should consider alternative finishes for the exterior facade.
- Consider many types of roofing materials.

- Instead of a flat roof and parapet walls, use a sloped roof system.
- Redesign complex elements and make them simpler to accommodate standard construction processes.
- Reduce the size and quantity of glass used.
- If gutters aren't necessary, get rid of them or develop a cheaper solution to manage water run-off.
- Choose external construction choices that require less time to install.
- Reduce the number of exterior perimeter walls by redesigning the floor plan.

Interior Construction Of The Building

Marketing agents should analyse the interior design of the spaces to verify that the floor plan layout possibilities are competitive in the market. The builder can look over the blueprints for structural improvements that can be made without changing the space's arrangement. The interior designer can look over the interior floor plans to see where less expensive finishes can be employed. Take into account the following:

- Use carpet instead of wood or tiles for a more cost-effective floor finish.
- Reduce the height of the floor to the height of the ceiling.
- Make use of low-cost plumbing fixtures.
- Make use of low-cost door hardware.

- Consider adopting less expensive heating and cooling options.
- Stack plumbing devices vertically to save water and sewerage plumbing distances.
- Instead of wallpaper, use paint.
- Rearrange the floor plan to reduce the number of doors and the length of walls.
- Use a different door.
- Use blinds instead of curtains to change the window treatment.
- Replace pricey paint colours with less priced paint.
- Reducing the number of electrical outlets is a good idea.
- Select equipment that does not necessitate the use of separate electrical circuits.
- Skylights should be removed.
- Instead of custom cabinetry, use standard cabinetry.

Design Of The Landscape

The landscaping design will be crucial to the development's final success since it improves curb appeal, which helps sell the finished product. You can reduce these expenditures by using fewer and smaller plants.

The landscape contractor can look through the plans and requirements while considering the installation and long-term maintenance costs. The landscaper might suggest changes that take these factors into account and the planting season.

Amenities

Amenities will always increase the development's costs and future operation costs, yet without them, the market may not choose this development above its competitors. The architect can look over the amenity designs for cost savings and ease of installation. In contrast, the marketing agent should look over the facilities to see whether they provide a competitive advantage.

Conclusion

In the early stages of design development, analysing and practising real estate economics can save a lot of time and money. Examining the cost after the working drawings, specifications, and tenders will lengthen the development process and, as a result, cost more in interest due to the later market delivery.

Because their experience and ingenuity will provide solutions to every challenge, the developer should effectively use team members in this process. Due to the sensitive personalities of the designers and the team's expectations to succeed, the developer must be an effective leader.

The architect's duty is to give design recommendations, the quantity surveyor's function is to keep track of costs, but the real estate developer is the one who sets the ground rules. One can accomplish this by thoroughly understanding your actual demands and the price you are willing to pay to have them met. You'll have a better chance of getting the development you want if you define design and cost parameters from the beginning.

Pave your success path with my Structured Property Development Courses.

FAQs

What is property development economics?

Developers who are looking to cut expenses and increase profits should consider how property development economics can help them. A 'cost reducing' mindset is usually prevalent in awful real estate developments, but a more cost-effective & cost-saving approach would be beneficial for all parties involved with the process!

Can economic growth help development?

Economic growth is the most efficient approach for decreasing poverty and raising living standards in emerging nations. As a result, solid economic growth supports human development, which encourages economic growth.