

Commercial Edge Week Two



Housekeeping

1. Please stay until the end to have your attendance marked
2. Keep your video on
3. Unmute if you'd like to ask a question
4. There will be quizzes and polls during the session



Week one recap

01 What's the opportunity?

02 Breaking down the steps to winning in commercial



Agenda

01 Commercial property lending

02 Servicing calculations



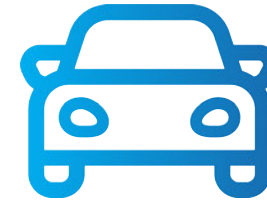
Commercial property lending

Easiest place to start?



Commercial property finance

- Similar to residential property finance
- Substitute residential property to commercial property
- Understand the customer/business behind the purchase



Asset Finance (vehicles)

- Quick turnaround times
- Most businesses have them
- Renew every 3 to 5 years

This is the time to get into commercial property lending

Historically it was challenging for clients to purchase or refinance a commercial property due to:

- High Interest rates - 5% p.a. plus
- Short loan terms - 10 to 15 years
- Low LVRs - maximum 65%
- Not many low doc options

Now brokers have access to many more commercial lenders which has led to the following:

- Rates from as low as 3% p.a.
- Loan terms of up to 30 years
- LVRs of up to 85%
- Various income verification options

Example of difference in repayments

Let's look at an example of a 500K loan then and now:

Then:

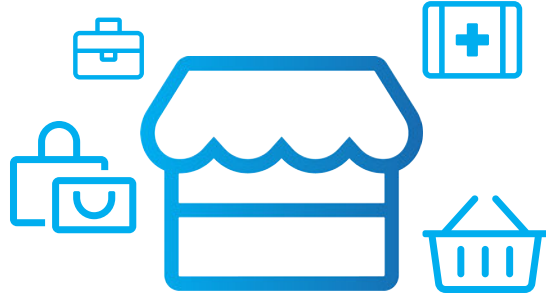
- Interest rate - 5% p.a.
- Loan term - 15 years
- Monthly repayments = \$3,954

Now:

- Interest rate - 3.5% p.a.
- Loan term - 30 years
- Monthly repayment = \$2,246

What is a commercial property?

Commercial property refers to real estate property that is used for business activities. Commercial property usually refers to buildings that house businesses, but it can also refer to land that is intended to generate a profit, as well as larger residential rental properties



Standard commercial property

- Retail
- Warehouses/factories
- Offices
- Medical practices
- Vacant land
- Simple tenancies (1 or 2 tenants)



Specialised commercial property

- Hotels, motels, pubs
- Service stations
- Childcare centres
- Shopping centres
- Income producing land
- Multiple/complex tenancies

Owner occupied vs. investment commercial property

- Owner occupied deemed properties exist when a business owner operates their own business out of a commercial property for which their business is the sole tenant or anchor tenant.
- Investment deemed commercial real estate properties are when a third-party tenant occupies the facility or where the operating entity uses less than 40% of the total square footage of the property.

Differences:

	Investment property	Owner occupied property
Cashflow consideration	Cashflow is first determined by rent	Cashflow comes from the operating entity
Structure of loan	Loan term matches the lease term	More flexibility around loan term

Investing in commercial property

Advantages	Disadvantages
Higher returns	Untenanted periods
Longer lease periods	Vulnerability to economic factor
Fewer ongoing expenses	Costly upgrades
Value adding activities	Lack of general knowledge and research

Goods and Services Tax (GST)

The rules surrounding GST on commercial property can be complex. It is recommended that customers seek professional advice prior to entering into any purchase contract.

Generally a purchase of a commercial property will attract a GST if the property is vacant, however if the property being purchased has an existing tenant who will continue to operate from the premises the GST will be avoided. The good news is your client is generally able to claim any GST included in the purchase price if:

1. They are registered for GST
2. They hold a tax invoice for the purchase
3. The property is being used to carry on an enterprise

GST applies if the seller (vendor) is registered or required to be registered for GST purposes

The GST will be refunded on the next BAS cycle (1-6 months)

What impact does this have on a purchase?

Commercial property in lending

- Typically lower loan terms (10-30 years)
- Higher interest rates (3% p.a. +)
- Lower LVRs (55% - 85%)
- Serviceability assessed via an Interest Cover Ratio (ICR) Model
- Complex structures are more common making serviceability more difficult to assess
- Alternate doc options available (full doc, lease doc, low doc, self dec)
- Valuations take an average of two weeks to complete
- Annual reviews are common in the \$1M+ space



Common Questions to ask?

- What Type of Commercial property is being purchased?
- Where is the location of the property?
- What is the premises currently being used for?
- What is the purpose of the purchase? Owner occ or investment?
- If Owner occ does the business cashflow support the purchase?
- If Investment what is the remaining lease term if any?
- IF no current lease, will there be a new lease in place prior to settlement?
- Is GST Applicable? Has this been included in PP?
- What LVR is required?
- When is the settlement date?



Servicing calculations

How to assess serviceability

Most lenders use an **ICR** and **Debt Service Cover Ratio**

$$\frac{\text{Total group income}}{\text{Total annual Interest}} = \text{ICR}$$

$$\frac{\text{Total group income}}{\text{Total annual Principal \& Interest}} = \text{DSCR}$$

EBITDA is used to identify income from trading business

Earnings

Before

Interest

Tax

Depreciation

Amortization

Let's use our Financial statement example to calculate EBITDA

Example of commercial property purchase

- Purchase price 700k
- Loan amount required 500K
- Interest repayments @ 3.5% rate is \$17,508 pa
- P&I repayments over 15 years \$53,625 pa
- Assumed P&I repayments for leases \$45,300 pa

$$\text{EBIDTA} = \begin{array}{l} \text{Earning before tax} \\ \text{Interest} \\ \text{Total depreciation} \end{array} = \$159,997 + \$10,249 + \$63,593 = \$233,830$$

$$\text{ICR} = \frac{\$233,830}{\$17,508 + \$10,249} = 8.42x$$

$$\text{DSCR} = \frac{\$233,830}{\$53,625 + 45,300} = 2.36x$$

Rent vs. loan repayments

Purchase Price	LVR	Deposit	Loan Amount	15 yr term	20 yr term	30 yr term
\$4,000,000	80%	\$800,000	\$3,200,000	\$27,004	\$22,926	\$19,186
\$3,500,000	80%	\$700,000	\$2,800,000	\$23,628	\$20,061	\$16,788
\$3,000,000	80%	\$600,000	\$2,400,000	\$20,253	\$17,195	\$14,390
\$2,500,000	80%	\$500,000	\$2,000,000	\$16,878	\$14,329	\$11,992
\$2,000,000	80%	\$400,000	\$1,600,000	\$13,502	\$11,463	\$9,593
\$1,500,000	80%	\$200,000	\$800,000	\$6,751	\$5,732	\$4,797
\$900,000	80%	\$180,000	\$720,000	\$6,076	\$5,159	\$4,317
\$800,000	80%	\$160,000	\$640,000	\$5,401	\$4,586	\$3,838
\$700,000	80%	\$140,000	\$560,000	\$4,726	\$4,013	\$3,358
\$600,000	80%	\$120,000	\$480,000	\$4,051	\$3,439	\$2,878
\$500,000	80%	\$100,000	\$400,000	\$3,376	\$2,866	\$2,399
\$400,000	80%	\$80,000	\$320,000	\$2,701	\$2,293	\$1,919

Purchase Price	LVR	Deposit	Loan Amount	15 yr term	20 yr term	30 yr term
\$4,000,000	65%	\$1,400,000	\$2,600,000	\$21,941	\$18,628	\$15,589
\$3,500,000	65%	\$1,225,000	\$2,275,000	\$19,198	\$16,299	\$13,640
\$3,000,000	65%	\$1,050,000	\$1,950,000	\$16,456	\$13,971	\$11,692
\$2,500,000	65%	\$875,000	\$1,625,000	\$13,713	\$11,642	\$9,743
\$2,000,000	65%	\$700,000	\$1,300,000	\$10,971	\$9,314	\$7,795
\$1,500,000	65%	\$525,000	\$975,000	\$8,228	\$6,986	\$5,846
\$1,000,000	65%	\$350,000	\$650,000	\$5,486	\$4,657	\$3,898
\$900,000	65%	\$315,000	\$585,000	\$4,937	\$4,192	\$3,508
\$800,000	65%	\$280,000	\$520,000	\$4,389	\$3,726	\$3,118
\$700,000	65%	\$245,000	\$455,000	\$3,840	\$3,260	\$2,728
\$600,000	65%	\$210,000	\$390,000	\$3,292	\$2,795	\$2,339
\$500,000	65%	\$175,000	\$325,000	\$2,743	\$2,329	\$1,949
\$400,000	65%	\$140,000	\$260,000	\$2,195	\$1,863	\$1,559

- Are you currently renting? Tell me about your lease terms?
- What are your plans after the lease? What is the impact if you were to break the lease?
- What would be the impact if you were to buy your own property? How would this impact your growth?
- Did you know based on your current monthly repayments, you could potentially afford a business loan \$x?
- If we got an approval in principal, would this help you get closer to your goal of owning your own commercial property?
- What is your wish list? Location, square meters, other i.e. overhead gantry, mezzanine, tilt panel

Next week

- 01 Westpac introduction and accreditation process
- 02 Benefits of Asset Finance for you and your clients
- 03 The process from start to finish
- 04 Westpac's online portal, DriveOnline

Contact us



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