

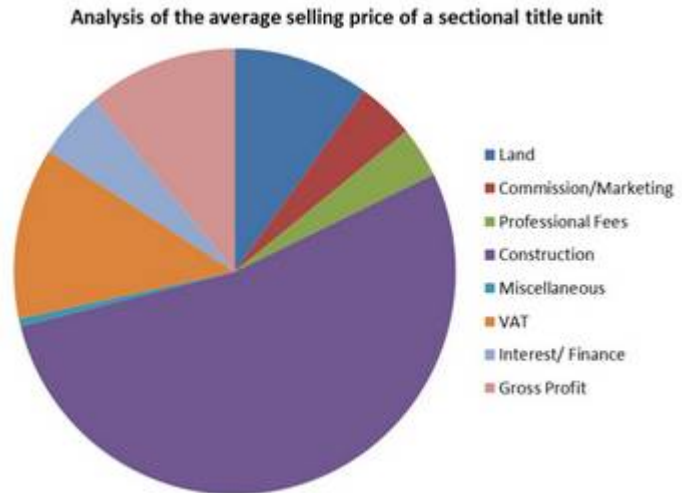
## NEW DEVELOPMENTS PUT THE SQUEEZE ON DEVELOPERS' PROFIT MARGINS

Published by SA Property News on: August 16, 2011

The profit margins of developers and contractors have been squeezed in order to bring new developments to the market during the economic downturn, says Colin Green, a director of Rabie Property Group.

Green says residential developments have been particularly hard hit following the downturn in the property market that most industry players started experiencing towards the second half of 2007.

“The gap between the price of existing and new stock remains high, and the introduction of the National Credit Act, together with the tightening of the banks' lending criteria, have made it difficult for many would-be buyers to access finance.”



*Pie chart showing an analysis of how sectional title prices are made up*

Green says that although the price of building materials has come down since the end of the boom labour prices have continued to escalate.

“There is very little building work taking place, which has resulted in margins coming under pressure. Some contractors are happy to secure work at cost just to pay their overheads, and hope to work smartly to make a small profit at the end of the contract. Current building prices are similar to the tendered rates of several years ago.”

Green says many buyers of new properties are unaware of the various components that make up the selling price of a unit.

“An analysis of several recent sectional title developments carried out by the Rabie Group is illustrated in the accompanying pie chart, and indicates where your money goes when buying a new sectional title apartment. Although the percentages vary slightly from one development to the next, they are surprisingly consistent for each development product. However, the percentages do vary between different types of development such as sectional title, group housing and single residential.

“Not surprisingly, construction costs account for the lion's share – 50 percent to 55 percent of the purchase price. There is no transfer duty on new properties as the prices include 14 percent VAT. The developer's profit is a variable that depends on how accurate the developer was in estimating the total development costs and predicting the selling prices. Gross profit, before overheads, ranges from about 9 percent to 13 percent of the purchase price.

“Land accounts for between 8 percent and 12 percent of the purchase price and includes development contribution fees, which are fees charged by the local authority as a contribution towards future infrastructure upgrades. Interest (holding costs) and finance charges account for 5 percent to 6 percent. This is historically low and is indicative of the low interest rate environment that we have enjoyed in recent times. With large scale developments that include a fair degree of repetition, professional fees, marketing and commission come in next at around 4 percent each. Miscellaneous costs such as council scrutiny fees, NHBC registration costs, insurance, audit fees, and legal costs, account for 2 percent to 3 percent of the selling price.”