Property Development Cashflow Examples

Rather than a series of cashflows determined by regular incoming rental income and regular outgoing, development cashflows are based around a series of sporadic outgoings and even more sporadic incomings. Rental income is no longer the key driver of the cashflows, which is heavily focused on costs. Despite these differences, there are similarities in structure with the Investment model, namely the concept of global and local inputs, interim calculations, cashflows and outputs. In addition to IRR, NPV and Worth, additional tools to evaluate the projects are also introduced, for example Profit on Cost Ratio (PCR) and Equity Multiple (EM).

Development cash flows have the advantage of being able to place income and expenditure within a time context. This allows the developer to distinguish between phased income items as well as calculate the interest on costs incurred accurately.

When building a development cash flow model the following should be kept in mind:

- Summary and inputs clearly distinguished, in their own separate areas and at the front of the model.
- Periodicity of cash flow is normally monthly as accounts are usually settled at the end of each month.
- Phased sales: sales brought forward improve cash flow.
- Separate costs into continuous and fixed date: this allows the modeler to distinguish one off costs that are known to occur at a particular time, such as planning fees from the general stream of construction costs.
- Delayed costs improve cash flow in the same way as income brought forward do. In particular costs that are delayed until income is received can be financed from this income. However careful attention must be paid to the measure of profitability used.
- Consider ownership structure: residuals usually assume 100% finance and include interest as a cost when setting or comparing the profit on cost ratio.

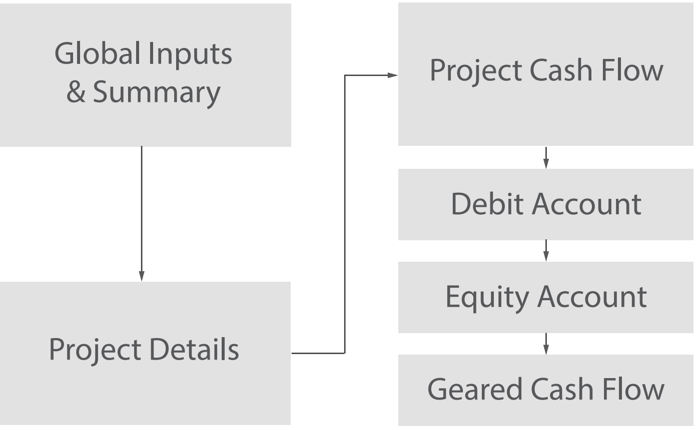
MODEL STRUCTURE

As with the investment model, the date series runs horizontally. We now also have, instead of tenant variable, project detail variables which should run down columns to the left with one unit/tenant per line.

Figure 1: below illustrates the best practice layout for the development model. The associated course model is set out on a monthly basis. The cashflow is for three years, which equates to thirty-six periods of one month each.

The model is laid out in the following way with single figure inputs and outputs on the left hand side and the cash flow models on the right hand side. The model exists entirely on one sheet reducing the demand on computer memory.

Figure 1: Development Model Layout



We can see that the model is, 'Project Details' and 'Project Cash Flow'. When we introduce external financing, we bring in three further sections; the 'Debt Account', 'Equity Account' and 'Geared Cash Flow'. These will be explained in detail in the following sections.