Advice for entrepreneurs: what you need to know about securing financing for commercial property

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Several advantages make owning commercial or business property a viable prospect for small businesses. These include the benefit of asset appreciation, enjoying full control over interior design and renovations, security of tenure and avoiding above-inflation rent hikes. As a first port of call, small and medium enterprise (SME) owners need to be aware of the various steps in securing finance for commercial property and to be as prepared as possible to put forward a strong application.

Shane Padayachy, area manager at Business Partners Limited

Commenting on this topic is Shane Padayachy, area manager at Business Partners Limited who explains that the process of acquiring funding for business property "involves more rigorous vetting procedures and due diligence than applying for residential property.

In general, small business owners need to ensure that their application will inspire confidence in the financier, providing assurance that the purchase is financially feasible both in terms of the future value of the asset and the track record of the business purchasing the business property."

Financiers interrogate funding applications on three fronts: the state of the client's business, the viability of the transaction and the value of the property being acquired. Research and preparation are therefore key to successfully securing funding for commercial property. This relates to both how supporting documents and information on the business itself are collated and presented, as well as aspects that position the property in a favourable light as a good investment.

Apart from the documents required for FICA purposes, SME financiers and other financial institutions will require a detailed business plan as part of the application. This will need to be accompanied by a strong finance proposal backed by the business' annual financial statements.

As Padayachy asserts: “Some of the factors that financiers consider when reviewing funding applications include the credit history of the business and in many cases also the credit record of the owner.

Arguably the most important aspect that will be reviewed is the state of the business’ cashflow management. As our quarterly SME Index continues to demonstrate, cashflow remains the number one challenge for South African SMEs. As such, applications need to shed light on whether consistent, adequate and sustainable cashflow will be maintained over the loan period and how any potential shortfalls will be subsidised.”

In terms of the property itself, financiers may require applicants to provide information on the history and current condition of the property, including aspects such as whether it has been well maintained and if any major structural issues have been identified. Required documentation will include the purchase agreement from the estate agent or current owners, as well as any rental agreements that may apply to current or future tenants (in the case of plans to sub-lease).

“Apart from its financial viability, the location of the property will play a pivotal role in the decision-making process. Financiers will consider aspects such as crime rate, the reliability of public services in the area, proximity to competitors, the condition of surrounding buildings and whether any new developments are planned in the area. Entrepreneurs also need to ascertain whether the property complies with municipal regulations. This will influence the ability to raise finance as well getting the property properly insured.” advises Padayachy.

After the research and preparation process has been completed, SME owners are advised to review their options in terms of the interest rates and repayment options made available by banks, lenders and independent financiers.

The major factors that entrepreneurs will need to consider at this stage will be lending rates, term, the size of the bond and any related fees. In terms of fees such as administration, payments to attorneys for legal services and VAT, SME owners need to enquire as to whether these costs will be incorporated into the loan amount or whether they will become payable separately.

The distinction between commercial and residential properties will have bearing on the loan term, given that business property is regarded as an income-generating asset. Generally, therefore, banks will expect loans to be paid off faster than residential bonds.

“Although SME owners may intuitively think of banks as their primary option for funding, we encourage established entrepreneurs to consider alternatives,” says Padayachy.

Our research and experience have shown us that in the initial stages of securing financing for commercial properties, one of the major pain points for small businesses is accumulating enough capital for a deposit. A deposit-free funding option may be more viable and accessible. In these cases, SME owners need to understand the conditions of a deposit-free loan and how it differs to traditional financing.”

As an example, Padayachy references Business Partners Limited’s offering, tailored for SMEs who are considering purchasing commercial property. One available option is a transaction that offers an advance of up to 100% of the financing required, subject to conditions relating to the nature and usage of the property. These deals may involve an increased cost of funding to obtain the finance but allows the Business to invest cash flow into the operations which will in turn stimulate growth and increase profits.

“Owning their own business premises, developing residential complexes for resale or student accommodation is within reach for many SMEs provided they find the right financier. We encourage SME owners to explore their options, review their budgets and weigh up the long-term benefits of different funding options. Investing in commercial property can be a powerful next step for an entrepreneur, so it’s important to make a well-informed decision based on your current reality and your projections for the future,” concludes Padayachy.

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