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Bridging loans prove versatile

By Tanya Powley

Bridging loans have been increasing in popularity since the economic downturn, as more buyers find it difficult to sell a property quickly, and end up needing to finance a new home before their sale proceeds come through. But bridging finance is now being used by property investors, as well, to fund stages of their projects.

As demand for rental properties continues to rise, a growing number of property investors are taking out bridging loans to purchase properties that need to be refurbished or redeveloped – because these typically do not qualify for buy-to-let finance until there is a full rental valuation.

Bridging loans can also be used when buying a property at auction or when buying a house that is unmortgageable until it has been renovated.

"The purpose of raising finance is very varied," explains Mark Abrahams of West One Loans, a bridging lender. He says some customers will also use a bridging loan for non-property purposes – such as short-term capital raising and project finance.

However, borrowers considering a bridging loan should seriously consider the costs involved and their exit strategy, brokers warn.

"The biggest downside to traditional bridging is the costs – it's not unusual to have a 2 per cent entry fee and a 1 per cent exit fee, and a monthly interest rate of 1.25 to 1.5 per cent," warns Nigel Bedford of Largemortgageloans.com.

Aaron Strutt of Trinity Financial, the mortgage broker, says it is possible to secure access to cheaper bridging loans if a client has a significant amount of equity in a property.
United Trust Bank charges 0.85 per cent a month, with a 2 per cent arrangement fee. West One Loans will typically charge around 1 per cent a month in interest, but it will arrange lower interest rates for "top quality" borrowers.

Other bridging lenders include Precise Mortgages, Dragonfly and Omni Capital.

But, in addition to the interest rate, experts say that having a clear exit strategy is one of the most important considerations. “Many borrowers are too focused on getting the property and they do not have a good enough plan to repay the debt,” notes Strutt.

Even when there is an obvious exit strategy, it can carry a high degree of risk, brokers add. If the exit route is to find a buyer for the property, there can be no guarantee of that this will happen – or at the right price.

In addition, most mortgage lenders now require borrowers to have owned a property for six months before they can remortgage it, warns Strutt. “There are a limited amount of lenders that will let you repay the bridging loan straight away, so this makes it very hard to take out a mortgage to repay the bridging loan,” he adds.
Borrowers should therefore carefully consider whether they really need a bridging loan, says Simon Checkley of Private Finance. Traditional mortgage lenders such as private banks can often provide attractive short-term lending deals for wealthy clients – at a lower cost than normal bridging finance – by allowing them to release some of the equity in their existing properties to put towards a new purchase.
“If borrowers can access funds through another avenue, this may be worth exploring,” notes Strutt.

For those simply under time pressure, though, bridging can provide an useful avenue. Many bridging lenders say they have the ability to complete on a deal with 24 hours, and many lenders do not have a maximum loan size. If a deal is being held up, it can be a valuable facility, says Strutt. “Our clients typically use bridging loans to secure new properties while they wait for another sale to go through – it enables them to complete on a new residential home or investment property.”