Bridge Loans – the Instrument of the Real Estate Professionals

From Dr. Roger Stettler, Tanguy Bonbled, 09.02.2021

Professional real estate investors are increasingly using bridge loans in order to act quickly and flexibly when opportunities arise in the market. The main advantage of this instrument is the short time between loan application and loan disbursement, which gives investors a considerable advantage when sourcing properties. Additionally, the investors gain time to look out for the best financing in the market at their convenience. This - and the usually short terms - more than compensates for the higher costs of this instrument.

Bridge Loans – features

Bridge loans are loans with a short maturity, usually less than 6 months. In connection with real estate investments, they are usually mortgage-backed. They are normally repayable at any time without additional costs. Interest rates are typically in the range of 0.5% to 1% per month, supplemented by a one-off arrangement fee. Bridge loans are usually arranged through specialised intermediaries. They have the needed contacts to find the right lender for the real estate investor. In addition, well-positioned intermediaries have the know-how to analyse the project, draw up the necessary loan agreements and handle the transaction in a coordinated manner with all parties involved, such as public authorities, specialised lawyers, etc. Experienced intermediaries have a short lead time. With qualified intermediaries, the turnaround time for suitable transactions from the loan application to the disbursement is very short, and usually amounts to a few days, even for large loan amounts.

Tanguy Bonbled, Senior Consultant and Head Investments

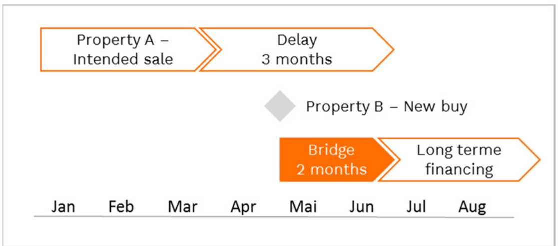
Successful property purchase - price, speed, deal safety and discretion

Attractive real estate properties with good yields and/or upgrading potential are in greater demand than ever. The probability that interest rates will remain very low (in some cases negative) for the foreseeable future is forcing investors to engage in the real estate market with sustainable positive returns. In addition to the price, factors such as the speed of processing a transaction, the chance that an agreed sale can be realised, as well as discretion, are central for the sellers of real estate. Professional property buyers who are considered reliable and fast regularly gain access to more attractive properties. Bridge loans are playing an increasingly important part in creating and maintaining this reputation.

Liquidity management

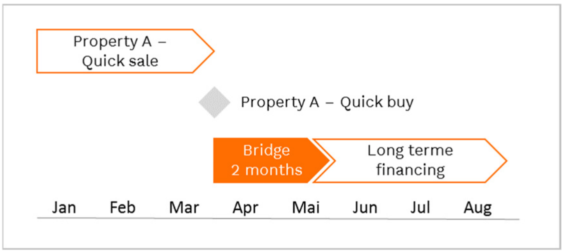
Diversified, larger real estate portfolios dispose of very stable cash flows. Accordingly, it is not necessary for investors - especially in a negative interest rate environment - to hold large liquidity reserves. If the opportunity arises to expand the portfolio in a short time - or if a property is to be sold to finance another property - considerable short-term liquidity bottlenecks regularly, which can be optimally solved by using bridge loans. The following typical cases are in the focus.

Example 1: Delay in property sale



According to the plan, property A is to be sold by 31.3. In order to finance the intended purchase of property B on 30.4. However, the sale of property A is delayed by 3 months due to a liquidity bottleneck at the buyer of property A. In order not to jeopardise or delay the purchase of the attractive property B, the short-term liquidity requirement is covered by the bridge. A part of the costs of the bridge is paid by a penalty of the buyer of object A.

Example 2: Quick purchase of an object



In order to raise liquidity for the acquisition of a company, a seller wants to sell a property (property A) quickly. The potential buyer has a lot of substance in his real estate portfolio, but cannot raise the required purchase price within a few days. He therefore takes a bridge loan and secures it with property A and properties B and C in order to finance the purchase. Subsequently, a long-term financing for the property is sought to be concluded a few weeks later.

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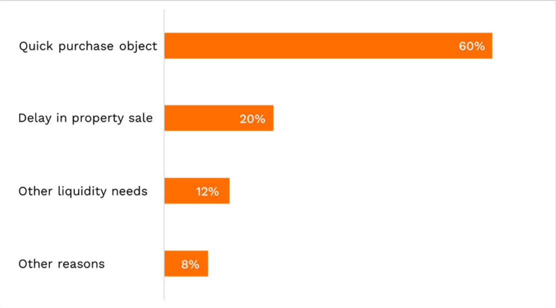
Optimisation of financing

With the use of bridge loans, the real estate investor buys time to evaluate the optimal financing from the market. Especially in the current market environment, it makes a lot of sense to find out the best potential lenders in order of having them offering various scenarios. Renegotiating of interest rates, loan-to-value ratios, amortisation and loan clauses are also part of today's business. All these financing steps take time for the real estate investor or his loan broker. Experience shows that choosing the right lender and the corresponding products more than compensate the costs of short-term bridging.

Reasons for Bridge Loans 2020



Source: 25 analysed bridge loans in 2020 with a total volume of CHF 130 million.

Risk-taking, fast lenders

Traditional lenders such as banks, insurance companies and pension funds do not play a major role in granting bridge loans. The processes and balance sheet structures of these providers are not aligned to the high urgency that characterises these loan cases.

Accordingly, lenders are found among family offices, highly liquid private individuals as well as some specialised funds and a few specialised banks. Often these companies also require (partial) guarantees from intermediaries. If the borrower is already known, in individual cases a credit decision and disbursement are even possible within a few hours.

In Switzerland only a few financing partners are in a position to meet the requirements regarding speed, real estate know-how and liquidity - and due to the requirements of Lex Koller, only local refinancing is practically possible, at least for residential properties.

Expensive, flexible solutions

Costs incur to the lenders due to the short-term provisioning of liquidity as well as the intensive examination by experienced experts in a short time. These costs are typically covered by the considerable interest rates of 0.5 % to 1 % per month - which, against the background of the short term, trigger manageable interest costs for the borrower. More significant are the one-time commitment fees of 1 % to 3 % - in return, however, the borrower has the right to repay the loan at any time without additional costs.

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The total costs of a transaction are thus within the range of normal real estate agent and broker fees.

Outlook: Demand high but limited availability

We observe that the demand for bridge loans today clearly exceeds the availability and that the general demand for loans is also growing faster than the supply of them. The reasons for this are increasing processing times for loan applications and more risk-averse lending by traditional refinancing partners as well as a professionalisation of real estate buyers.

In view of these developments, we expect the bridge loan market to continue to grow.

Hyrock is an independent mortgage expert for sophisticated private and institutional clients in Switzerland, with offices in Zurich and Geneva. In 2020, Hyrock realised a total of over CHF 850 million in financing solutions for its clients, with an average volume of CHF 7 million per transaction. Around CHF 250 million of these were mezzanine and bridge loans. www.hyrock.ch