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Castle Trust guide to

Bridging

Introduction

Modern day bridging is a world removed from what it was once known for. Bridging used to be seen as an expensive last resort, but as lenders have started to innovate, bridging has cleaned up its reputation. Smart lenders have developed news ways to help clients reach their financial goals and more secure funding models have made pricing more affordable.

Although bridging focuses on short-term successes, it often opens the door to a long relationship with your client and provides the opportunity to be their point of call for their longer-term finance needs.

This guide takes a look at some traditional and up-and-coming uses of bridging finance from across the industry, which may provide some food for thought in terms of growing your business.

Marcus Dussard
Director of Sales
Castle Trust

What is bridging?

Bridging is a short-term loan with flexible pay-back options, it often comes at a higher price than mainstream finance in order to allow clients to achieve short-term goals before moving to more sustainable finance plans.

Bridging requires the borrower to have a clear exit plan in place, so that the lender can confidently process their application with the efficiency required by the client. Speed tends to be an important factor in bridging finance, with clients typically looking to seize an opportunity or meet a short-term need before putting a more sustainable plan in place.

Modern bridging loans offer a degree of flexibility making them versatile for short-term projects and opportunities. Typically this flexibility is offered through a shorter ERC period than a standard loan or an agreed level of penalty free overpayments.

45%
average loan to value (LTV)

11
months average term

0.84%
average monthly interest rate

46%
regulated

Source: EY, UK bridging market study: A view for 2018 and beyond

Finding the right bridging product for your client

To find the right bridging loan for your client, you will need to clearly understand their circumstances. Bridging loans vary in features which can be selected to achieve the right result for your client.

Variable features include:

Terminal payment

- Open bridge
- Closed bridge

Repayment method

- Capital and interest
- Interest only
- Rolled-up interest

First or second charge

Finance options available

- Buy to Let bridging
- Commercial bridging
- Residential bridging
- Non-standard/unmortgagable properties

Popular uses for bridging finance

- Property refurbishment
- Auction finance
- Development exit
- Business use
- Tax bills
- Divorce settlements
- Chain break finance

Source: smallbusiness.co.uk, Common uses for bridging loans

Property refurbishment

A popular use of bridging finance is experienced landlords looking to purchase a property and use their own funds to make some improvements to the property, with a view to either to sell the property once the work has been completed, or to refinance onto a more affordable Buy to Let product. Each lender will have their own definition of light or heavy refurbishment, and many lenders limit their standard priced bridging products to light refurbishment so it's important have a transparent conversation with the lender.

Light refurbishment

Properties will often require some light refurbishment to improve their capital and rental value.

Light refurbishment typically includes:

- No planning permission
- Cosmetic improvements i.e. painting & decorating
- Fitting a new bathroom or kitchen

Heavy refurbishment

Some properties will require more TLC to get them turned around.

Heavy refurbishment typically includes:

- Planning permission or the need to involve certain building regulations
- Structural changes
- Extensions and conversions

The value of a new kitchen and bathroom

Squeezing an extra bathroom into a property is likely to cost between £2,500 and £6,000, but will typically boost the value by 5% – nearly £15,000 on the average home.

A new kitchen costs, on average, £8,000 to install but can typically add 6% to the property price - £18,000 on the average home.

Source: National Association of Estate Agents

Case study

A Buy to Let investor was looking to purchase a two bedroom maisonette in need of a new bathroom and some cosmetic improvements, before putting it on the rental market. The investor had the capital to fund the improvement required to increase the capital and rental value, however they wanted finance to purchase the property.

The purchase price of the property was £220,000, and Castle Trust was able to lend £150,000 on a roll-up basis meaning the investor didn’t need to make any monthly payments during the works. He was then was able to refinance over to a serviced Buy to Let product when the property was ready to be let out.

Auction finance

Bridging finance can be ideal for investors looking to meet the short deadlines of a property auction. With completion required within 28 days of the transaction, bridging finance provides the necessary turnaround times to secure the property.

Good things to have in place ahead of bidding in a property auction:

- An agreed level of finance with the lender
- An agreed level of refurbishment acceptable to the lender
- A clear exit strategy from the loan

Bid with confidence

It is important to make your circumstances clear to your lender so a pre-agreed level of credit can be set before heading into auction. Your lender will need to know any quirks of the property and the level of refurbishment required. Some lenders will provide bridging finance for heavy refurb properties, however it's always good to know what the boundaries are before going to auction.

Case study

Castle Trust was approached by a broker whose client had an interest in a property coming up for auction. The client had visited the property and had a good idea how much refurbishment work would be required, so their broker got in touch with their Castle Trust BDM to talk through the case.

An LTV of 68% was agreed with the broker and the client was able to successfully bid on the property and, after a swift exchange of paperwork on both sides, the client was able to complete the purchase in 19 days.

Development exit

Development exit loans can be particularly helpful to property developers who are approaching the end of their scheme and are getting ready to move to market with the completed properties. At this point in the development, cash flow can be a problem whereas the developer will have assets in abundance.

Development schemes don't always go to plan and developers can find themselves in a market where their completed properties would not achieve the anticipated values. At this stage, the developer may choose to refinance onto a Buy to Let product if yields are more favourable.

However, for developers looking to sell, bridging can buy extra time whilst finding suitable buyers for the properties, allowing them to ride out a market dip and achieve the anticipated values on the completed properties.

Refinancing a development finance facility in order to sell the completed properties has a clear exit strategy in place making it an attractive product for lenders. Aside from buying the developers more time, a bridging product can be the the alternative to substantial rate loadings and penalty fines from the development finance lender.

Fact: The UK development bridging market is expected to grow from £2.1bn in 2018 to £3.2bn in 2022.

Case study

The client was a property investor who had recently completed a development and had identified a plot of land right for his next project. In order to seize the opportunity, the client explained to his broker that he wanted to free up capital from the completed property whilst he waited for the sale to go through. The client's broker worked with Castle Trust to facilitate a bridging loan of £227,500 at 70% LTV, allowing the client to proceed with the new project.

Source: Mintel Forecasts, cited in EY

Business use

The number one reason businesses fail is cash flow, so it's unsurprising that cash flow is the main contributor for business use bridging loans. Business owners, who are looking to use the loan to grasp an opportunity or pay off an urgent expense, are more understanding of the premium cost of bridging finance because they recognise the value of flexible pay back options and quick turnaround times.

Popular reasons for bridging for business use	
Funding growth	New plant/offices/machinery
Covering credit terms	On large contracts that don't pay out on day one
Seasonality	Additional staff and inventory for peak periods
Advertising	Lead generation

Another popular business use of bridging loans in the property market is using them to buy the investor time whilst completing paperwork and applications. For example, a landlord may purchase a short-term lease property with the intention of extending the lease to add value in order to sell or refinance the property. Alternatively, a property investor may buy a property to obtain planning permission in order to carry out extensive development work; the exit strategy for this being development finance.

Case study

A client was starting a recruitment company and needed short-term funding of £110,000 to cover costs until the revenue from candidates placed was received (6 months after appointment). The broker arranged a first charge bridging loan for the full amount on her unencumbered property, valued at £160,000, allowing her to establish the business without a long-term finance commitment.

Source: TotallyMoney Buy-to-Let Yield Map, 2018

Tax bills

One of the biggest selling points of bridging finance is that it is there for clients with a need for capital but only for a short period of time. It serves as a stepping stone when cashflow can be a problem for asset-rich clients.

For self-employed clients, tax bills won't be a gradual expense like for those in steady employment. Whilst most will account for their tax bill throughout the year, some may need short-term help to meet a tax demand whilst their funds are tied up in an investment project.

Fact: Since 2014, HMRC have issued accelerated payment notices (demands for payment within 90 days) totalling £8.7bn.

Case study

A self-employed consultant was surprised to receive a tax demand from HMRC as a result of an historical miscalculation. Despite planning his taxes well, he was unprepared for the bill of £30,000 and needed prompt access to the funds to avoid penalty payments. The client's existing high street lender was not able to offer the funds, but the broker sourced a second charge bridging loan secured on the client's main residence, bringing the total LTV to 55%.

Source: Financial Times, HMRC accused of carelessness over disputed tax demands

Divorce settlement

Like many other uses for bridging finance, divorce settlements can cause a short-term requirement for capital whilst affairs are settled between parties. Although it may not be its primary use, bridging finance can be an ideal solution in these circumstances due to the short ERC periods, which for many lenders can be as little as three months, giving your client flexibility to sort their financial affairs during a difficult time in their life.

Tip: Find a lender that can commit to moving quickly

Divorce is one of the most stressful events someone can go through, so a broker's top priority should be to ease the stress of the financials as much as possible for their client. This means finding a lender that communicates effectively and can swiftly deliver a smooth customer journey for your client.

No more love lost

Lenders view bridging as a stepping stone to help clients move onto longer-term finance plans. Using a bridging product to solve a short-term need of divorce settlement could be the start of a new relationship with that lender, with some lenders offering existing clients preferential rates.

Case study

During their relationship, Mr and Mrs Cross built up a Buy to Let portfolio. The properties were held in joint names, but Mrs Cross ran the business, including selecting and refurbishing the properties. Therefore, it was decided that Mrs Cross would take ownership of the properties after the divorce.

With an imminent court deadline, Mrs Cross needed to refinance the portfolio quickly. Her broker suggested a Castle Trust bridging product to ensure that the funds were released on time and that she would avoid having to go to court.

With the ERC only applicable for the first three months, Mrs Cross was able to refinance the portfolio penalty free shortly afterwards.

Chain break finance

With so many factors involved in a chain, they're vulnerable to breaking so bridging offers an option to protect parties from missing out. Whether your client's chain is breaking, or they want to break away from a slow moving chain, bridging finance can be the lifeline in a situation that would have otherwise fallen apart.

The biggest benefit of bridging in chain finance is it removes the dependency on another party to allow your client to achieve their goals, be that speed of completion or a buyer dropping out of the chain.

Case study

A portfolio landlord was restructuring his portfolio and had found a buyer for his £2m central London rental property. He intended to use the proceeds to purchase a higher yielding student accommodation block in Birmingham city centre worth £2.5m.

Just before both sales went through, the buyer of the London house pulled out but the student flats needed to complete before the landlord could secure a new buyer. In order to preserve the chain and avoid losing the Birmingham property, the client used his available funds, supplemented with a bridging loan of £1,700,000 at 70% LTV, to complete the sale.

Get in touch

At Castle Trust, we understand that time is of the essence for short term finance cases, that's where conversations with brokers in the early stages can make the difference in delivering timely finance for your clients.

If you would like to learn more about Castle Trust's bridging products, or if you have any bridging cases you would like to discuss, please get in touch.

Get in touch with your BDM

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Important information

Loans are subject to status, terms and conditions. The customer must repay the loan by the end of the term. If the customer has not repaid the loan by the end of its term and either does not have sufficient savings or is not able to arrange another mortgage, then they will need to sell their property. Property may be repossessed if the loan is not paid when due. This communication is for authorised intermediaries only. This information has not been approved for use with customers and is not intended for public or customer use.

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