4 types of bridging finance and how they can help SMEs navigate uncertainty

Small to medium-sized enterprises (SMEs) can face various financing issues, especially in the initial lifecycle of their business. Structured as a short-term loan agreement with flexible terms, bridging finance is a useful financial tool that can help carry SMEs through short-term periods of uncertainty.

Image supplied

“This form of short-term finance is a useful way for SMEs to bridge cashflow gaps, fund operational needs or start expanding a business. Often, businesses also face the issue of delayed payment from their clients. The flexibility and fast access of bridging finance can support SMEs in terms of day-to-day operational cashflow in this instance,” says Tom Stuart, chief marketing officer at Lulalend.

Having a clear understanding of bridging finance and its various forms is imperative in helping business owners understand which options are most suitable for their needs.

1. Closed bridging finance

Closed bridging finance is a short-term loan that is issued by a lender to a borrower for a fixed term. This type of bridging finance tends to be more accessible because lenders have a higher level of certainty for the repayment of loan, since the set terms are agreed to beforehand.

2. Open bridging finance

Open bridging finance adds an element of flexibility for lenders. The terms of the loan do not stipulate a fixed date for repayment, which can be useful for businesses that face uncertainty. However, a setback of bridging finance is usually a higher interest rate owing to the uncertainty around the repayment period of the loan.

3. Debt bridging finance

Debt bridging finance is useful for businesses who need temporary, short-term finance to cover operational costs while a larger, long-term finance agreement may be pending. While this solution can be helpful for a smaller business that needs to cover costs in the short term, it is crucial to have a clear understanding of the repayment and interest structure of the loan to avoid exacerbating financial difficulties.

4. Equity bridging finance

Equity bridging finance usually takes the form of venture capital or private equity investment for equity in exchange for funds. In this instance, a venture capital investor would supply funding for a lender while the lender raises equity financing. This is a useful way for a lender to avoid accumulating high-interest debt.

“These various bridging finance options available to SMEs can help address their unique challenges. By taking a careful, strategic approach to bridging finance and its unique benefits, SMEs have a financial lifeline to help keep their operations functional during periods where cashflow might be dried up”, concluded Stuart.