MANAGING INTEREST RATE RISK WITH SMALL BALANCE BRIDGE LOANS

by Matt Zonies

856-470-3200 | contact@bluestoneloans.com | bluestoneloans.com | @bluestonecommercialcapital

---

Interest rate risk is generally defined as the risk that changes in overall interest rates will negatively (or positively) affect the value of an investment. The risk can be assumed by investors, lenders and even borrowers.

In the private real estate credit space, one way to mitigate risk is the sale of loans to aggregators. These aggregators purchase groups of loans from private lenders and then securitize the loan portfolio by issuing securities to institutional investors. The originating lender is able to offload the risk to the aggregator and recycle capital at the same time, thereby offering liquidity through the sale of loans and enabling them to originate more loans with that capital.

For lenders that choose to hold loans on their balance sheet, another way to reduce interest rate risk is by originating floating rate loans, which fluctuate alongside changes in interest rates. This can benefit lenders in a rising rate environment, but also hurt them during a rate cutting cycle. Pricing floors, or minimum interest rates on a loan, can protect lenders against this. However, pricing floors can also make it more difficult for lenders to originate loans, as the borrower bears a disproportionate share of the interest rate risk.

Bridge loans (typically 12-36 month terms) offer a unique opportunity for both borrowers and lenders to reduce their interest rate exposure by originating shorter duration loans at a fixed rate. This structure offers the borrower and lender a degree of certainty during the term of the loan. The lender can more accurately predict the return on investment, and the borrower can predict the total cost of the loan. Both parties bear a certain level of interest rate risk during the loan term; the lender benefits from a reduction in rates and the borrower benefits from a rise in rates.

Loan extensions present another opportunity to manage interest rate (and credit) risk from a lender's perspective. If the borrower wishes to extend the initial loan term, lenders will often charge an extension fee and increase the interest rate. This serves a dual purpose: 1) There is an opportunity cost incurred by the lender during a loan extension. The capital that remains outstanding to the borrower could otherwise be redeployed by the lender to another borrower and generate more fees; and 2) It compensates the lender for taking on additional interest rate risk in the form of duration risk. The lender is committing to a fixed return for a longer period of time. Increased risk requires increased return. That being said, it is assumed the lender is only offering loan extensions to performing borrowers, so the increased duration risk is being mitigated by the borrower's track record of timely payments.

MEET YOUR DEDICATED UNDERWRITING TEAM

Bluestone Commercial Capital LLC was founded in 2017 as a private credit manager focusing on small balance commercial real estate financing. Through its private fund vehicle, Bluestone originates short-duration loans secured by first liens on commercial real estate and non-owner occupied residential real estate assets.

Matt Zonies
President

background includes financial analytics, commercial real estate, tax and corporate law. Prior to founding Bluestone, he served as counsel to a family-owned private real estate lender. Matthew graduated from The College of New Jersey with a BA in Finance and earned a JD from Rutgers Law School.

Dan Hampton
EVP of Originations

Dan oversees portfolio management and new deal flow for all loan products on the Bluestone platform. Dan spent the first part of his career at an investment banking firm in New York where he participated in raising over $300MM in debt for institutional fund managers.

Janis Niv
Originations Associate

Janis joined Bluestone in 2025. Her responsibilities include underwriting, structuring and closing loans through Bluestone's balance sheet and capital markets products. Janis brings prior experience at a construction lender in Philadelphia where she originated and serviced RTL loans for developers operating in underserved neighborhoods