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Unsecured loan a better option than a credit card?

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Unsecured loans are sometimes overlooked by consumers when considering borrowing options. Many borrowers first go for a credit card to satisfy their immediate financing needs. Unsecured loans are a viable alternative to credit cards that can offer value and save money.

When comparing credit offers

Look at the total repayment over the full loan term

- Comparing interest rates only can be misleading because it doesn't include all fees and the cost of credit life insurance

As unsecured loans represent more risk to lenders, interest rates are often higher than those of loans secured by assets.

Structurally, credit cards and unsecured loans are similar. They are both forms of credit and they both require a monthly repayment. What differ are the features and fees.

Unsecured Loans (Also called Personal Loans)

Loan term:	Is finite
No Collateral – no need to sell off assets:	Only backed by a borrower's promise to repay
Fixed interest rates:	Don't change over loan term. You can budget and plan better
Repayment schedule:	Debt will eventually be repaid and you're not be tempted to spend

Credit Cards

Time period:	Revolving line of credit
Qualification Criteria:	Need a good credit history and minimum income requirements
Variable Interest Rates:	Linked to the prime lending rate and risk profile of the applicant
Minimum repayments:	Minimum repayment required each statement period leads to rolling of debt

Which way to go?

Personal Loans have a fixed term and more money cannot be borrowed without a new loan application. Credit cards can be used repeatedly up to their credit limit.

Many credit cards offer extended warranties, insurance coverage or discounts which unsecured loans do not.

Note that each application for either a personal loan or a credit card reflects on your credit report. Multiple enquiries may indicate unsustainable borrowing habits and can be a red flag to creditors.

Who should consider a personal loan? As no collateral is required, this may be the only option for people who don't own homes or other tangible assets. The application process is fast and simple and suits borrowers who need money quickly. A fixed interest rate provides stability with unchanging monthly payments. If successful with the application, the money is usually transferred directly into a nominated banking account.

As the personal loan is only backed by the borrower's promise to repay, the applicant's credit history is very important. Documentation must be provided to show sufficient income to service the repayments and to support an expenditure schedule.

Unsecured personal loans can be obtained from banks, finance companies and other registered credit providers. It makes sense to get quotes from a number of competing lenders. You should compare repayments, fees, loan term, penalties and APR.

APR = Annual Percentage Rate (Also note representative annual percentage rate which assumes nil repayments get made). This includes all charges to the consumer, meaning all costs of the credit including interest and other charges that are directly connected with the credit agreement. The European Union and USA require the calculation to be disclosed in any offer of credit.

In South Africa the National Credit Act stipulates that the following information must be disclosed: the instalment amount; number of instalments; total amount of all instalments (including interest, fees and insurance); residual or final amount payable; and the interest rate and other credit costs.

Unscrupulous lenders will emphasise the speed and easy access rather than the price.

Look out for shady lenders! There are plenty of firms ready to exploit desperate people.