Secured vs Unsecured Loans:
What is the Difference?

By Suzette Ransome

Secured Loans

For a secured loan, lenders take collateral (such as a house or car) to encourage borrowers to pay back the loan on time. After all, the threat of losing your home or automobile is a strong motivator to repay the debt and avoid foreclosure or repossession.

If you have previously been denied an unsecured loan, it does not imply you have to be turned down for a secured loan These are distinct products, and lenders are usually less cautious with secured loans than with unsecured loans. This is because the lender is guaranteed security with a secured loan. Although this enhances your chances of acceptance, the penalties of non-payment are grave as your property could be at risk if you don't pay back your secured loan. It is therefore important to be sure you can afford the repayments before you take out a secured loan.

When choosing which secured loan to apply for, don’t only look for the one with the lowest monthly instalment. You must also examine other aspects, such as the interest rate, fees, the term (length) of the loan, and whether you are required to maintain an insurance policy on the collateral. Before you sign the contract, it is vital to know exactly what you agree to because a loan is a major financial commitment.

Secured loans, sometimes called homeowner loans or second charge mortgages, can be used to decrease the risk to the lender by leveraging the equity on your house. Other secured loans use collateral, such as a vehicle or equipment, to secure the loan. Secured loans are useful for a wide range of applications including rehabilitation and upgrading, acquisition of cars, and debt consolidation. A secured loan is generally for a greater amount than an unsecured loan, and may be offered with a payback period of three to 25 years.

Benefits of a secured loan:

- Lowered monthly instalments might reduce your financial hardship.
- Depending on your circumstances, you can borrow larger amounts.
- More people, including ones with poor credit histories, are eligible.
- You can utilize them for many objectives, including debt consolidation.

Disadvantages of a secured loan:

- You might end up paying more towards the end, particularly if you picked a long period of payment.
- If you don't comply with the repayment schedule, your house or vehicle could be in jeopardy.
- Lenders will consider using just a specific quantity of equity in your property, so perhaps you cannot borrow as much as you believe.

Unsecured Loans

What's an unsecured loan?

The main distinction is that many more people can apply for an unsecured loan; you don’t have to be a homeowner or able to afford collateral, such as a vehicle. However, as a general rule, you need at least a good credit score to be approved. Some lenders might consider a poor credit loan, but repayments and interest rate would both be higher.

If you are not eligible for an unsecured loan, an alternative such as a mortgage loan might be a possibility. Variously unsecured loans, from short-term loans with a payback period of only 30 days, to longer-term unsecured loans of up to five years, are available.

You are not putting your property at danger when you get into arrears with an unsecured loan. This is because the lending arrangement does not use your property as collateral.

Benefits of an unsecured loan:

- Not only homeowners with a mortgage and equity are eligible to apply.
- You can borrow both small amounts and rather large sums
- Many forms of unsecured loans provide a broad range of repayment options and interest rates.
- If you get into arrears, your house or vehicle will not be in danger.

Disadvantages of an unsecured loan:

- You need good credit to qualify, especially for the best interest rates.
- If your loan amount is lower, the interest rates may not be available to view before applying.
- Repayments and interest rates per month are usually higher than secured lending.

While secured and unsecured loans both offer a means of borrowing money, the products are significantly different. You may wish to consider getting independent financial advice before you apply if you are unsure about what is best for your circumstances.