

The basics about loans

Putting money aside and earning interest on it is always better than borrowing, even though sometimes borrowing cannot be avoided. For example, to buy something that costs \$100, you could save \$95 and use the interest you earn to get to your target amount. Or you could borrow the \$100 and pay another \$7 or \$8 in interest – or maybe \$18 if it goes on your credit card!

Smart money management is like giving yourself a pay rise, because your money can go a lot further. However, when you do need a loan, you want one on the best possible terms. To do that you need a good credit rating and a good banking record.

A good credit record means being a reliable customer and paying what you owe on time. Merchants and lenders share information with credit and debt collection agencies, so when you successfully clear a loan or debt, your standing as a reliable customer should be reinforced.

However, if you default on a loan or get into arrears, that will almost certainly end up as a black mark against you – and it can take a long time to re-establish your good name.

The golden rule with borrowing money is that if you are having trouble with the repayments, approach the lender and try to negotiate an extension or deferral of payments. Don't wait for them to take action to sort out your overdue account.

As well as a clean credit record, a good banking history is an asset. Suppose you want to take out a mortgage to buy your first home. As well as having the deposit, say 20% or 25% of the purchase price, some lenders will also want evidence of your savings record for the last one or two years. Their reasoning is; if you have a good savings record, you're likely to be a good manager and therefore a better bet than someone who is used to spending their money as quickly as they earn it.

It's exactly the same in business. If you need to extend your overdraft to tide you over during a lean patch, the bank is more likely to help out if you can show you have managed the business responsibly and successfully.

Ironically, the more you need a loan, the less a bank will want to give you one. On the other hand, if your financial situation looks good, they'll be only too pleased to advance you a loan to expand your business, take a holiday, buy a new car, etc. It's often quipped that a bank will happily lend you an umbrella when it's fine, but then take it back when it starts raining!

At the end of the day, a lender is in the business of lending to make money – and they don't do that by being a charity.

ENDS

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