

# Loan- Types, Advantages & Disadvantages



## Introduction

Nowadays loan is a common word because everyone is familiar with it in one or other way. In simple language loan is an amount which is lending from one person, entity or a financial institution to another person, entity or financial institutions.

## Meaning:

- A loan is the lending of money from one source to another source for a specified period.
- A loan is a debt given by an organization to another organization with an interest rate.
- In a loan, a borrower borrows money from the lender with a certain rate of interest and pay back it in future.
- The main activities of financial institutions like banks, NBFC, is to provide a loan to the customer.

## Types of loan

There are mainly five types of loan.

### 1) Secured loan

- In a secured loan, a borrower pledges some asset as collateral like property, car etc.
- A mortgage loan is a type of secured loan used by a customer. In a secured loan, a money is using to purchase a property.
- If in case the borrower fails to pay back the loan amount a lender has legal right to possess the collateral security and recover the money.

### 2) Unsecured loan

- In the unsecured loan, a loan is not secured against any of property of the borrower.
- This type of loan is available from the financial institutions like banks, NBFCs and other private institutions.
- In unsecured loan interest rate depends on the lender and the borrower and the rate of interest in an unsecured loan is always higher than a secured loan.
- There is more risk associated with the unsecured loan that a customer may not pay back an amount.
- In case of insolvency, unsecured lenders are the second priority to pay the money.
- An unsecured loan may be one of the following:
  - Personal loans
  - Credit card debt
  - Bank overdrafts
  - Line of credit
  - Unsecured bonds

### 3) Demand loan

- Demand loans, as the name suggests, are short term loans.
- Short term loan means there is no fixed time to repay an amount it means it can be repaid at any time.
- A demand loan uses the floating rate of interest to charge an interest.

- A demand loan may be a secured or unsecured.

#### 4) Subsidized loan

- In a subsidized loan, an interest rate is reduced by subsidy.
- This type of loans is given to the students for education purpose.
- Sometimes in the subsidized loan the whole amount of interest is paid by the government.

#### 5) Concessional loan

- A concessional loan is also called as a "soft loan".
- A concessional loan is given either through below market interest rates, by grace periods or a combination of both.
- This type of loans is given by the developed countries to the developing countries.

### Advantages & Disadvantages

#### Advantages of loan:

- Nowadays loans are easily available to anyone by stable financial sources like banks, NBFCs, private institutions.
- Nobody can take undue advantage of the borrower in any emergency.
- There various types of loan as per the needs of the customers.
- Due to competition among the financial institutions, a customer gets to benefit from this competition like lower interest, more time to repay.
- Sometimes there are government schemes like saving in tax, lower interest rate if in a specific time period loan is taken

#### Disadvantages:

- There is a lengthy process to get a loan it requires various types of documents, proof, witness and many other things. So, it takes a longer time to section a loan.
- Sometimes the documents and many other things demanded by the institutions are so unnecessary that it makes inconvenient to the client.

- A loan is never granted in the full amount. There is always a ratio of the amount applied for a loan and the amount to grant. It may be 80:20 ratio, it means a bank gives 80 percent loan of the applied amount.

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