Glossary of Loan Terms

Whether you are seeking business or personal financing, we want to be sure you are familiar with the language of loans. The greater your knowledge the quicker you can move along the application process. Remember each loan varies in length, interest rates and repayment requirements.

Credit Corporation's goal is to help you find the best loan for your needs and provide the guidance that gets you to the most positive outcome.

Types of Loans:

Secured Loan

A secured loan is any type of financing that requires collateral to secure it. Common examples are mortgage and equipment loans, which use the property you're purchasing as collateral. Secured loans may also require a personal guarantee.

Personal Guarantee

A personal guarantee is a provision a lender puts in a business loan agreement that requires owners to be personally responsible for their company's debt in case of default. Lenders often ask for personal guarantees because they have concerns over the credit history, age or financial stability of your business. Personal guarantees are common in unsecured debt agreements.

Unsecured Loan

Unsecured loans, on the other hand, are not backed by collateral and are considered riskier as a result. An unsecured loan is supported only by the borrower's creditworthiness, rather than by any collateral, such as property or other assets.

Term Loan

Debt financing that you take out and repay over a set period is considered a term loan. Term loans may have fixed or variable interest.

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Fixed Interest Rate

A fixed interest rate stays the same over the life of your loan, regardless of changes in the economy.

Floating (Variable) Interest Rate

Floating or variable interest rates will change depending on changes in the market. The rates will go up or down at intervals specified in your loan contract.

Loan Considerations:

Underwriting

This is when a lender assesses the risk it assumes by allowing you to borrow money. Underwriting is part of the vetting process lenders perform before they approve or deny a loan.

Collateral

This is an asset – like property or something else of value – used to secure a loan. The lender will seize the assets you put up for collateral and keep them if you fail to pay back the loan.

Assets

This is any property of monetary value that can be used as collateral – including real estate, equipment, stocks or bonds.

Loan-to-value (LTV) ratio

Lenders use this calculation to assess the financial risk of extending a secured loan to your business. It weighs the amount of the loan against the value of your collateral.

Early Settlement Fee

Lenders charge this fee to offset the loss of interest when the borrower pays down all or a large part of a loan before the loan maturity date.

Working Capital

This is how much money your business has on hand to use for its day-to-day operations.

Cash Flow and Income Statements

Cash flow is the amount of money that goes in and out of your business over a certain period. Income is your company's total revenue, minus expenses. Lenders analyze cash flow statements and income statements to assess the risk they're taking by lending you money.

Age of business

This is how long your company has been in business. It's another factor lenders consider before deciding whether or not to approve your loan request. Many lenders require you to be in business for at least two years before they will lend you money.

General Terms:

Balloon payment

This is a large sum of money paid to the lender at the end of the loan term. If a loan is not fully amortized over the loan term, there is a large balance remaining before the loan's maturity date that the borrower must pay.

Grace period

This is a set amount of time after the due date – usually 5 days – when interest doesn't accrue on your debt and you aren't penalized for late payments.

Amortization

Amortization is the process of paying off debt through regular installment payments. Each payment covers a portion of the loan's interest and principal balance.

Loan Default

A loan goes into default when a business or person fails to make loan payments. Lenders can notify credit bureaus when a loan is placed in default, which will have a sharply negative effect on a business credit score.

Lien

This is a legal claim that gives the lender the right to seize assets that the debtor pledged as collateral if they default on the loan.

Loan Principal

The total amount you borrow, or the current balance of your loan, is the principal. This is used to calculate interest. This is the amount of money borrowed in a loan. It does not include interest or other fees attached to the loan.

Maturity

This is the end of a loan term when the final principal and interest payments are due.

Refinancing

When you refinance a loan, you pay off a loan by taking out a new loan that offers better interest rates or longer terms, thus lowering your monthly payment.

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