More Options to Choose From...

A Simple Guide to Online Installment Loans and Lines of Credit

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Introduction and Summary

When it comes to financial services, it's good to have options. The multi-billion dollar payday lending industry is progressively growing, with more and more people in demand for a short-term loan. But as the industry continues to develop and expand, so does the product. Shortly after making the jump to the Internet, online lenders began to realize that borrowers wanted, and needed, more options from which to choose. While payday loans are a great short-term solution, they don't offer enough longevity and flexibility for the borrower. As a result, online lenders introduced two new products: installment loans[i] and lines of credit.[ii]

46.9%

46.9 percent of families have taken out or currently own some sort of installment loan

(Federal Reserve Board, 2009)

According to the 2007 Survey of Consumer Finance and its 4,422 respondents:

- 46.9 percent of families have taken out or currently own some sort of installment loan
- 56.2 percent of installment loan borrowers are between 35-44 years old
- 56.2 percent of installment loan borrowers hold a managerial or professional position (Federal Reserve Board, 2009)

Credit cards, a widely familiar type of line of credit, are used by millions across the country:

- Cardholders have an average of 3.5 credit cards
- U.S. consumers accounted for an estimated 609.8 million credit cards in 2008
- The average age at which a U.S. consumer under the age of 35 first obtained a credit card is 20.8 years old (Foster et al., 2010)

56.2 percent of installment loan borrowers are between 35-44 years old

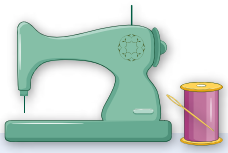
(Federal Reserve Board, 2009)

So what exactly is an online installment loan and a line of credit? With an installment loan, borrowers are lent one lump sum up front, where as with a line of credit, borrowers can withdraw money as needed up to their available credit limit. In terms of repayment, installment loan payments are fixed and follow a specific schedule over the loan's duration, while line of credit payments depend on the total that has been withdrawn. In other words, the more a line of credit borrower withdraws, the more they pay each month. While these products may be new, the concept of "installment lending" is generations old.

A Long, Long Time Ago

Installment lending is one of the earliest forms of consumer credit. Around

1850s — Installment financing first used for furniture, pianos, farm equipment and sewing machines (Anderson, 2012)



1890s — Singer's successful "dollar down, dollar a week" sales tactics leads to rise in installment financing (Davies, 1976)

1950s — Credit cards become popular post World War II (Stephey, 2009)

1980s — First line of credit appears in the form of a home equity line of credit (Cavanaugh, 2007)

2000s — First online installment loan and line of credit issued at CashNetUSA

the 1850s, when mechanization[iii] and the mass production of consumer products were on the rise, four products were the first to take advantage of installment financing: furniture, pianos, farm equipment and sewing machines. All of these products represented social superiority — living without a piano oftentimes meant a family was of lower class descent. As a result, consumers worked with businesses to purchase these items in installments as a way to improve their social standing (Anderson, 2012).

One of the biggest companies to first embrace installment financing was Singer Sewing Machines. Before sewing machines, it took an average of 14 hours to produce a shirt. With a sewing machine, it reduced the labor time to one hour. By the 1890s, the company's aggressive "dollar down, dollar a week" sales tactics, along with its easy payments, propelled Singer Sewing Machines into one of the nation's most successful companies. Singer's success ultimately paved the way for other companies to embrace installment financing for their line of electronics, jewelry and automobiles (Davies, 1976).

Although the history of a line of credit doesn't run quite as deep as an installment loan's, it's just as important. Since the 1980s, consumers have borrowed home equity lines of credit[iv] (HELOCs) to help pay for an assortment of things, including education, home improvements and medical bills (Cavanaugh, 2007). Credit cards, on the other hand, have been around since the 1920s, but it wasn't until after World War II that they became popular. After Diners Club released its first card in 1950, almost 20,000 Americans were already carrying it a year later (Stephey, 2009).

Today, installment loans and lines of credit can be applied for via the Internet. They offer higher loan amounts and more flexible funding and repayment options than payday loans. Plus, they are collateral free. Instead of waiting in long lines at storefronts and being required to fill out extra paperwork, borrowers can apply for and receive their money directly into their bank account typically in the span of one business day. But how exactly do they work?

How Online Installment Loans Work

1. Apply online

2. Get approved

3. Get funded

4. Repay in installments

How Online Installment Loans Work

Installment loans, a type of personal loan, are medium-term loans that are repaid gradually in installments and typically carry a higher loan amount than a payday loan. With online lenders, installment loans are secured through the Automated Clearing House (ACH),[vi] the same process that employers use to deposit checks directly into their employees' bank accounts. When an online application is submitted, the lender will begin its review process and verify that all of the applicant's information is accurate — this could take as little as five minutes or up to a few days, depending on the lender and the information the borrower provides. Once a borrower is approved, money is deposited directly into their

bank account and debited in installments over the course of the loan's duration instead of in one large payment, such as with a payday loan.

How Online Lines of Credit Work

Lines of credit, or personal lines of credit, provide borrowers with more versatile funding and repayment options than other short-term credit products. A line of credit essentially acts as a bank account that a borrower can withdraw money from anywhere at anytime. Once a borrower submits an application, the lender will begin its review process and first verify all of the applicant's information. Similar to a payday and installment loan, this verification process could be instant or take up to a few days, depending on the lender and the information provided. Once an application gets approved, the applicant will receive a credit limit and be able to request advances to be deposited into their bank account as many times as they want up to their available credit limit.

How Online Lines of Credit Work

1. Apply online
2. Get approved
3. Receive credit limit
4. Withdraw money up to credit limit
5. Repay in gradual payments over time

Eligibility Requirements

Prequalifying for an online installment loan or line of credit is easier than one might think. Although each lender has different applicant requirements, most borrowers typically only need to have an active checking account, have been employed for at least one month, be a U.S. citizen or permanent resident and at least 18 years old. Once a borrower submits an online application, the lender will begin its review process and determine whether or not the applicant is eligible for the product, which could be instant or take up to a few business days.

The Essentials of a Top Online Lender

In addition to payday loans, some online lenders now offer installment loans and lines of credit to give prospective borrowers a wide array of financial products to choose from. With higher loan amounts and more flexible funding and repayment options, borrowers can easily select a product that is more suitable for their current situation. But how does a borrower know which lender to choose from when they are constantly being fed the same marketing propaganda from every direction? Here are a few elements borrowers should look for to help separate the good from the bad and the ugly:

- Speed — It's important to choose an online lender that can deliver an installment loan or line of credit in a quick and efficient manner. A fast online lender will typically deposit money into a borrower's checking account by the next business day from the time they are approved for the loan. If a lender's funding time takes longer than that, keep looking.

- Repayment options — It's good to have different repayment options when paying back an installment loan or line of credit. Installment loans are especially convenient because they allow a borrower to spread his/her payments over several months instead of one large payment, as with a payday loan. Flexible lenders will work with a borrower and offer a few repayment options, including making minimum payments or partial payments. The more a lender is willing to work with a borrower, the better.

- Customer service — An online lender willing to help a borrower will always offer customer service Monday – Friday. An online lender that is willing to go above and beyond to help a borrower will provide 24/7 customer support via phone, email or online chat.

• Trust — As beneficial as the Internet has been to the lending industry, it has also allowed many unlicensed lenders to take advantage of first-time borrowers. In 2005 alone, over 8 million Americans fell victim to fraud,[viii] identity theft[ix] and various other scams (Federal Trade Commission, 2007). If a lender doesn't provide licenses for each state it offers installment loans or lines of credits in, look elsewhere.

Over **8 million Americans** fell victim to fraud, identity theft and various other scams in 2005.

(Federal Trade Commission, 2007)

Debunking Installment Loan and Line of Credit Myths

With so many misleading installment loan and line of credit reports circulating the Internet these days, it's difficult for a borrower to differentiate fact from fiction. Dedicated to advancing financial empowerment for consumers through small dollar, short-term loans, the Community Financial Services Association of America (CFSA)[x] conducted a simple and honest examination of the payday lending industry in an effort to debunk all myths associated with short-term credit options, which can include installment loans and lines of credit. Here are a couple:

Myth: The short-term credit industry impacted the larger economy and was partly responsible for the financial crisis.

Reality: When other financial institutions required billions of dollars in government bailouts during the recent recession, online lenders received no bailout but were still able to offer consumers installment loans and lines of credit, despite the risk.

Myth: Anti-lending activists have consumers' best interest in mind.

Reality: While anti-lending activists claim to have a consumer's best interest in mind, many of their actions work to eliminate the already small number of short-term and flexible funding options available, leaving consumers with little to no options for covering their emergency expenses (CFSA, 2012).

Conclusion

Despite lending more than $40 billion in 2004 (Melzer, 2009), the payday lending industry determined that there was a demand for bigger and more versatile financial options. Payday loans sufficed for those in need of small and short-term loans, but what about borrowers who yearned for higher loan amounts and more flexible funding options? As a result, installment loans and lines of credit were introduced to provide borrowers with different products for different situations. A medium-term loan that typically offers a higher loan amount than a payday loan, an installment loan is best suited for those who seek a cash advance for a longer time period. A line of credit, on the other hand, allows a borrower to request money whenever they want, wherever they want, up to their available credit limit. But despite their differences, both products share one ultimate purpose: to help all types of borrowers — male, female, young, old — bridge their credit gap.

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Glossary

[i] **Installment loan** — A medium-term loan, usually with a higher loan amount than a payday loan, which is repaid gradually in installments.

[ii] **Line of credit** — A loan that offers more flexible funding and repayment options than other short-term credit products. Borrowers only need to apply once and can request money as often as they want up to their available credit limit.

[iii] **Mechanization** — The replacement of human operators with complex machinery to expedite production.

[iv] **Home equity line of credit (HELOC)** — A loan in which the lender agrees to lend a maximum amount within an agreed period, with the borrower's home serving as collateral.

[v] **Collateral** — Serves as protection for a lender against a borrower's default.

[vi] **Foreclosure** — The process of taking a mortgaged property as a result of the owner failing to make payments.

[vii] **Automated Clearing House (ACH)** — An electronic network for financial transactions in the United States.

[viii] **Fraud** — An intentional act of deception intended to damage another individual.

[ix] **Identity theft** — Stealing another person's identity and pretending to be them.

[x] **Community Financial Services Association of America (CFSA**) — A national organization established to promote laws and regulations that protect consumers while preserving their access to credit options.