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Debt Consolidation Loans Pros And Cons

A debt consolidation loan is a type of a personal loan that allows consolidating multiple credit card debts or other debts into one. The new loan may be subject to a lower interest rate, thus reducing the interest payments. Moreover, the borrower makes only one monthly payment which makes household budgeting an easy task.

While debt consolidation comes with many advantages, getting a consolidation loan is easy only on condition that the borrower meets some requirements. First, the monthly income has to be over a specified amount so that the borrower is able to meet the monthly payments. To that purpose, the applicant for a debt consolidation loan should be working, prove another source of income, or both. The credit union or bank evaluates the financial situation of the borrower and his ability to pay off the loan. The borrower should bring last year's tax returns, together with the most recent pay stubs when applying for a debt consolidation loan. The applicant's financial situation may require that a cosigner guarantees the loan. He/ she will be responsible for the repayment of the loan if the original borrower is unable to service it. In other cases, collateral may be required such as a house, car, or another valuable.

In Canada, consolidate loans can be obtained for various types of debt, such as credit card debt, personal loans, and others. Typically, only unsecured loans are consolidated as opposed to mortgage loans, which are secured ones. The debt consolidation loan may be offered with a fixed or variable interest rate. The loan will be offered with a lower interest rate, but it has to be paid off over a longer period. A larger amount may have to be repaid in the long run. Moreover, if he/ she continues using multiple credit cards, the risk of incurring more debt is high. In this case, the crediting institution will not be as sympathetic to late and missed payments.

Debt consolidation loans are typically offered to trustworthy borrowers, meaning that the latter have serviced their debts in a timely manner. Homeowners are considered more stable compared to borrowers who rent. Even if the homeowner defaults on the loan, the bank can always foreclose on the home. The lender can sell the property and use the proceeds to pay off the loan. Borrowers who cannot offer collateral will be able to consolidate only a part of their loans. Those who have $40,000 of equity in their home will not have a problem to consolidate $25,000 of debt.

Some banks will also prefer that the applicant has a certain debt to income ratio. The borrower's monthly disposable income should be between ten and fifteen percent of his gross income.

How to consolidate your debt is easy with this debt consolidation guide.