Boosting Your Odds of Loan Approval



A personal loan provides a flexible means of funding various types of expenses. These loans can range from a low amount of $600 to the six digits. Borrowers may use personal loans to subsidize medical bills, car repairs, wedding expenses, funeral costs, and home renovations. They may also use the money for other purposes, such as debt consolidation.

The criteria for loan approval can vary for each lender. However, there are strategic ways to maximize your chances of getting approved.

In this article, I will discuss the most effective tips to boost a typical personal loan applicant’s shot at approval. These tips include working on your debt-to-income (DTI) ratio, increasing income, finding ways to prequalify before formally applying, and improving your credit score.

In addition, to help borrowers who might not be eligible for a conventional loan, I will differentiate traditional loans from VA direct and VA-backed veterans home loans.

While such loans still require income and credit for the loan amount you wish to borrow, they may offer better terms than regular personal loans from a credit union, private bank, or mortgage down payment. I will explain the advantages of getting a VA loan, which includes the omission of a down payment requirement 90% of the time.

Through this article, readers will become aware of their options to get the best possible shot at the loan they need to accomplish their life goals.

By the Numbers

As of the third quarter of 2023, Americans collectively held $241 billion in personal loan debt, reflecting a 3.9% increase from the previous quarter's $232 billion and a notable 14.8% surge from the same period a year ago.

This indicates a significant upward trajectory in personal loan obligations. The number of Americans with personal loans has also risen, reaching 23.2 million in the third quarter of 2023, compared to 22.0 million in the preceding year. This marks a 5.5% year-over-year growth, underscoring the increasing prevalence of personal loans among the populace.

Personal loan debt also makes up 5.0% of non-housing consumer debt, constituting 1.4% of the overall consumer debt landscape in the third quarter of 2023.

In contrast, credit card debt among Americans stands at a substantial $1.079 trillion, forming 6.2% of the total outstanding debt. These figures highlight the varied composition of consumer debt and the distinct role personal loans play within it.

The delinquency rate for personal loans, defined as payments being 60 days or more overdue, currently stands at 3.75% as of the third quarter of 2023. This marks a decline from the previous year's rate of 3.89%, indicating a positive trend in loan repayment behavior among borrowers.

The average personal loan debt per borrower has reached $11,692 in the third quarter of 2023, showcasing an increase from the average of $10,749 observed a year earlier. This uptick in individual debt highlights the evolving financial landscape and the growing reliance on personal loans to address financial needs.

Notably, most borrowers (52.9%) opt for personal loans to consolidate debt or refinish credit cards. Home improvements are the second most common reason, accounting for 7.5% of personal loan purposes. This insight sheds light on the diverse motivations behind individuals seeking personal loans and the financial challenges they aim to address through this financial instrument.

Approval Boosters: Understanding What's Required

Personal loans are a type of unsecured debt that borrowers may use for various purposes, such as consolidating high-interest credit cards, paying for medical expenses, car repairs, wedding expenses, funeral costs, or funding a home improvement project.

Unlike secured loans, personal loans do not require collateral, which means the lender relies on your creditworthiness and income to determine your eligibility and interest rate.

However, getting approved for a personal loan is not always easy, especially if you have a low credit score, a high debt-to-income (DTI) ratio, or a limited income. Lenders use different criteria to evaluate your loan application, such as your credit history, income, employment status, and existing

debts. These factors help them assess your ability and willingness to repay the loan on time and in full.

If you do not meet the lender’s minimum requirements, however, you may face rejection or unfavorable terms, such as a higher interest rate or a lower loan amount. This can affect your financial goals and credit score, as each hard inquiry from a lender can lower your score by a few points.

Improving your success rate

Fortunately, there are some effective ways to boost your chances of getting approved for a personal loan. Here are some tips to consider before you apply:

1. **Work on your DTI ratio:** Your DTI ratio is the percentage of your monthly income that goes toward paying your debts. The lower your DTI ratio, the better your chances of approval, as it shows the lender that you have enough income to cover your loan payments and other expenses. To lower your DTI ratio, you can try to increase your income, pay off some of your existing debts, or avoid taking on new debt.
   For example, if you have a monthly income of $4,000, and a monthly debt payment of $1,000, your DTI ratio is 25%. If you can pay off $200 of your debt or increase your income by $200, your DTI ratio will drop to 20%, making a difference in your loan approval.
2. **Increase your income:** Another way to improve your loan eligibility is to increase your income. Prospective borrowers may do so by asking for a raise, finding a side hustle, or selling some of your unwanted items. A higher income can also lower your DTI ratio and show the lender that you have more financial resources to repay the loan.
   For example, if you have a monthly income of $4,000 and a monthly debt payment of $1,000, your DTI ratio is 25%. If you can increase your income by $500 through a raise

or a side hustle, your DTI ratio will drop to 18%, which can improve your loan terms and interest rate.

3. **Prequalify before applying:** Prequalifying for a personal loan is a process that allows you to check your potential interest rate and loan terms without affecting your credit score. This can help you compare different lenders and find the best offer for your needs. Prequalifying also shows the lender that you are a serious and qualified borrower, which can increase your chances of approval.
   For example, if you prequalify with three different lenders and get offers ranging from 10% to 15% interest rate and from 12 to 36 months repayment period, you can choose the one that suits your budget and goals the best.
4. **Improve your credit score:** Your credit score is one of the most important factors that lenders consider when evaluating your loan application. A higher credit score indicates that you have a good credit history and that you are responsible with your debt payments.

To improve your credit score, you can try to pay your bills on time, keep your credit card balances low, dispute any errors on your credit report, and avoid applying for multiple loans or credit cards within a short period.

For example, if you have a credit score of 650 and improve it to 700 by following these tips, you can save hundreds or thousands of dollars in interest over the life of the loan.

These are some ways to improve your chances of getting approved for a personal loan. By working on these factors, you can show the lender that you are a reliable and trustworthy borrower who can repay the loan on time and in full.

Remember to shop around and compare different offers before applying for a personal loan, as this can help you find the best deal for your situation.

When all else fails

While the above four tips work well for most applicants, to assure success with their personal loan applications, they might not work for everyone. For instance, what if your employable skills won't easily qualify you for a higher-paying job? So, does that mean you can't boost your chances for approval?

Well, the good news is that you still have one more strategy that pushes you over the approval hurdle: Apply with a co-applicant!

Applying for a personal loan with a co-applicant can significantly enhance your chances of approval by presenting a stronger financial profile to lenders. When you apply for a loan, whether it's a personal loan, mortgage, or any other type of credit, the lender assesses your creditworthiness and financial stability. Here's how having a co-applicant can be beneficial:

1. **Overcoming the Low-Income Hurdle:** Lenders often consider both applicants' combined income and assets. This can increase the overall financial strength of the application, making loan approval a more likely outcome. If one applicant has a strong credit history or a high income, it can compensate for any weaknesses in the other applicant's financial profile.
2. **Addressing Creditworthiness Issues:** If your co-applicant has a higher credit score than you do, it can positively impact the overall creditworthiness of the application. This may result in a lower interest rate and better loan terms. Lenders may be more willing to approve a loan when a co-applicant has a solid credit history, reducing the perceived risk.
3. **Improving Debt-to-Income Ratio:** Lenders assess the debt-to-income ratio to determine your ability to manage additional debt. Having a co-applicant with a steady

income can help improve this ratio, making the application more favorable.

4. **Offering Better Collateral and Security:** A co-applicant can provide additional assets to secure the loan if the loan requires collateral, as in the case of secured loans. This can be reassuring for lenders, as it reduces their risk in case of default.
5. **Shared Responsibility:** With a co-applicant, both parties share responsibility for the loan. This shared responsibility can give lenders confidence in the repayment capability, as it makes both applicants legally obligated to repay the loan.
6. **Introducing Flexibility in Qualification Requirements:** Some loans may have specific qualification requirements that can be challenging for an individual to meet. Having a co-applicant can provide flexibility, as the combined strengths of both applicants may fulfill the necessary criteria.
7. **Enhancing Negotiation Power:** Having a co-applicant can strengthen your position when negotiating loan terms. Lenders may be more willing to make concessions or offer better terms when they see a robust financial partnership.

WORDS OF CAUTION: While applying with a co-applicant can improve your chances of loan approval, it’s crucial to consider the implications for both parties involved carefully. Clear communication, trust, and a shared understanding of the financial commitment are essential when entering a co-application arrangement.

Traditional Vs. VA-Direct Vs. VA-Backed Home Loans

As indicated earlier in this post, borrowers may use traditional loans for various purposes, including to help finance the purchase of a loan. However, veteran members of the military have recourse to two additional types of loans that they may tap into to finance the purchase of a home.

These include VA (Department of Veterans Affairs) Direct and VA-Backed Veterans Home Loans.

Understanding the Differences

Traditional loans and VA loans (including VA Direct and VA-Backed Home Loans) differ in terms of eligibility requirements, the entity providing the loan, and specific benefits associated with each type of loan. Understanding these differences may help with making the right choices, when it comes to applying for a loan.

This knowledge may also help boost your chances of approval when you apply for the right product.

Eligibility

Traditional loans, often offered by banks and mortgage lenders, are available to a wider (compared to VA loans) range of borrowers. Eligibility is typically determined based on creditworthiness, income, and other financial factors. There are no restrictions on the availability of these loans to a particular group of individuals, which are available to the broader public.

VA loans assist eligible veterans, active-duty service members, and certain surviving spouses in obtaining home financing. VA loans are available to those who meet specific service requirements, such as a minimum length of active-duty service.

Entity providing the loan

Private lenders, such as banks and mortgage companies, may offer traditional loans. The government does not insure or guarantee such debt.

The Department of Veterans Affairs guarantees or directly provides VA loans. The government directly funds VA Direct Loans, while private lenders provide VA-backed loans, but the

VA guarantees them. The VA guarantee reduces the risk for lenders, allowing them to offer more favorable terms to eligible borrowers.

Down payment and mortgage insurance

Conventional loans may require a substantial down payment, and private mortgage insurance (PMI) is often necessary if the down payment is less than 20%.

VA loans are known for offering competitive terms, including the possibility of zero down payment for eligible borrowers. Additionally, VA loans do not require private mortgage insurance, which can be a significant cost savings for borrowers.

Interest rates

Interest rates for traditional loans are based on the borrower's creditworthiness and other financial factors. Rates may vary between lenders.

VA loans often feature competitive interest rates. The VA's guarantee makes lenders more willing to offer favorable rates to eligible veterans and service members.

Dissecting the differences

As you can see from the summary above, the VA loan program offers many benefits over traditional personal loans that can help you achieve your dream of homeownership. But what do these differences mean, and what financial impact do they have on your home-buying decisions?

Let's unpack some of the financially impacting features to help you understand those distinctions:

1. **No down payment requirement:** You can buy a home without making any down payment in most cases. This can save you thousands of dollars upfront and make homeownership more

affordable.

For example, if you want to buy a home worth $240,000, you would need to pay $48,000 (20%) as a down payment for a conventional loan. But with a VA loan, you can buy the same home with zero down payment, saving you $48,000.

2. **No mortgage insurance requirement:** You do not have to pay any monthly or annual fee for mortgage insurance, which can lower your monthly payments and save you money over time. Mortgage insurance is a type of insurance that protects the lender in case you default on your loan. Conventional loans have a mandated component of mortgage insurance if your down payment is less than 20%. The amount of mortgage insurance depends on your loan amount, loan term, and credit score.

   For example, if you have a $240,000 loan with a 30-year term and a credit score of 700, you would pay about $150 per month for mortgage insurance. But with a VA loan, you do not have to pay any mortgage insurance, saving you $150 per month or $54,000 over the life of the loan.
3. **Lower interest rate:** You can get a lower interest rate than you would get with a conventional loan, which can reduce your total cost of borrowing and save you interest over time. The interest rate is the percentage of your loan amount that you pay to the lender as the cost of borrowing. The lower the interest rate, the less you pay in interest.

   For example, if you have a $240,000 loan with a 30-year term and a 3% interest rate, you would pay about $1,011 per month and $124,265 in total interest over the life of the loan. But if you have the same loan with a 2.5% interest rate, you would pay about $948 per month and $101,384 in total interest over the life of the loan. That means you would save $63 per month or $22,680 over the life of the loan with a lower interest rate.
4. **Easier qualification:** You can qualify for a VA loan with more flexible credit and income requirements than what

you would need for a conventional loan. This can make getting approval easier when it comes time for you to apply for a loan to buy a home.

The credit score is a number that reflects your credit history and how likely you are to repay your debts. The higher the credit score, the better your chances of getting approved for a loan and a lower interest rate. The income requirement is the minimum amount of income that you need to have to afford your monthly payments and other expenses. The higher the income requirement, the more difficult it is to qualify for a loan.

For conventional loans, you typically need to have a credit score of at least 620 and an income that is at least 28% of your monthly debt payments (including your mortgage). But for VA loans, you can qualify with a credit score as low as 580 and an income that is at least 41% of your monthly debt payments (including your mortgage).

5. **One-time funding fee:** You only pay a one-time funding fee to the VA when you get a VA loan. This fee helps cover the cost of the VA loan program and reduces the burden on taxpayers. The funding fee varies depending on your type of service, type of loan, down payment amount, and whether you have used a VA loan before.

   You can pay the funding fee upfront or roll it into your loan balance. Some borrowers are exempt from paying the funding fee, such as those who receive VA disability compensation or are surviving spouses of veterans who died in service or from a service-connected disability.

   For example, if you are a first-time VA borrower who served in active duty and are getting a purchase loan with zero down payment, your funding fee would be 2.3% of your loan amount. That means if you have a $240,000 loan, your funding fee would be $5,520. You can either pay this amount upfront or add it to your loan balance.

Based on the above (hypothetical) example of a $240,000 loan,

compared to a traditional loan, a loan through the VA loan program may potentially save (or help defer) borrowing cost by nearly $125,000. That saving may potentially increase by nearly $5,500 more if you receive VA disability compensation.

Parting Thoughts

A personal loan offers a versatile solution for funding diverse expenses. Individuals can utilize personal loans to cover various costs, including home purchases. The approval criteria for loans can differ among lenders, leading to some applicants not meeting the qualifications. Nonetheless, there are strategic approaches to enhance the likelihood of approval.

Moreover, active-duty and retired members of the armed forces, who may not be eligible for a traditional loan, could access VA direct and VA-backed veterans home loans.

While these loans still necessitate sufficient income and a favorable credit history for the desired loan amount, they may present more favorable terms compared to standard personal loans offered by credit unions, private banks, or mortgage down payments.

The tips laid out in this post will boost your odds of loan approval for traditional personal loans, as well as VA direct and VA-backed veterans home loans.

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