



How to Make High Interest Loans

"The most powerful force in the universe is compound interest" -Albert Einstein

Don't you wish for a happy medium between the high risk of the stock market and so-called "high yield accounts" that are safe, but only give you 4-5% interest? I'm going to show you the tips that have helped me generate an average interest rate of 21.33%* on my money with medium risk! (*21.33% is meant solely to represent my average interest rate at the time of writing this article, and is not a guarantee of your results.)

The main part of the secret is a site called Prosper.com. Prosper.com is a site, started by Chris Larsen, who also started "E-Loan", that specializes in person-to-person lending.

What is "person-to-person" lending? The concept is very similar to eBay. Instead of a seller trying to sell a product to a buyer, you have a borrower asking for a loan from a lender, and instead of bidding the price of an item up, you are bidding the interest rate down. The interest rates you can receive on the site range from 6-29%!

Are you interested, but worried that you don't have enough to loan to someone? You don't have to loan the entire amount! Most loans are actually made by dozens of people each lending as little as \$50!

As a matter of fact, making several small loans is a great way to protect your money. Would you rather lend \$1,000 to one borrower or lend \$50 to each of 20 buyers? If the \$1,000 borrower defaults, you've lost \$1,000. If one of the \$50 borrowers default, then you've lost \$50, and you still have \$950 working for you!

In this form of lending, Prosper.com examines the borrower's credit information to decide if the loan is warranted. If they approve of the loan's conditions, the loan goes up for auction. If the lenders fully fund the loan, then Prosper.com approves and makes the loan, and pays each lender their share of the interest and principle (and late fees, if any) as it is payed.

Prosper makes their money two ways. They charge a 1-2% closing fee to the borrower, and a 0.5-1% loan servicing fee to the lenders. Both rates are determined by the borrower's credit score.

Here are some tips to help you get started:

- 1) Register for free at Prosper.com.
- 2) The three most important places for you, as a new lender, to visit are the [FAQ](#), ["How Person-To-Person Lending Works"](#) and ["Lend money to other people and earn interest"](#).

Read these sections carefully, so you know exactly how person-to-person lending works, and whether it is for you!



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- 3) Verify your identity and fund your account as instructed by the site.
- 4) Keep in mind that most loans will tie up your money for 3 years, so make sure you're not funding it with money you're going to need over that period of time.

5) As I mentioned earlier, make several loans to spread the risk of default. Sure, I'm repeating myself, but this is an important point!

6) Make loans and re-invest the money you make (re-read the quote from Einstein above)!

7) Every time you get your paycheck, set aside at least 5% of it as money you intend to loan! Remember, you should only loan money you can afford to lose!

Now, if you just did these few steps, you could easily beat those 4-5% "High Yield" savings accounts. However, I promised to show you how I make high-interest loans, and I will. I'll even show you how to minimize the risk!



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Here are the most effective ways I've found to make high-interest loans at [Prosper.com](#):

1) Prosper doesn't pay interest on the funds it is holding, so keep enough to make a few upcoming investments, while funds for loans you'll make farther down the road should be in an interest-bearing account elsewhere. When using an external interest-bearing account, try and use one that allows free transfers.

2) Don't bid on loans that are ending in more than four days. Why? If you bid on a loan that ends, say, 6 days from now, this will lock up your money for those 6 days. If you find a better loan that ends this afternoon, you may not be able to bid on it.

3) Look for loans that are being requested by businesses and individuals trying to expand their opportunities. Avoid loans which are requested as a way to get out of a bad situation.

4) When looking at businesses, do some research to see what type of profit margin is the average for that type of business. If the interest rate on which you're bidding is greater than the average profit margin, you'll probably want to avoid such a loan.

5) If the loan is sponsored by a group, look to see if the group leader themselves has bid on the loan. Groups of borrowers get a lower rating if one of their members defaults on a loan, so a group leader risking their own money is a strong sign of faith in the borrower's ability to repay the loan. If the group has a website, check that out. More information on a loan is a good thing!

6) Above and beyond the information provided by Prosper itself, you can find the history of any Prosper member by joining [Eric's Credit Community](#) for free. You can research your borrowers in further detail!



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7) Search for the borrower, and see if they have made multiple listings. This can be good or bad. Within Prosper, you can contact the borrower and ask questions. If other people would find the answers interesting, they'll often wind up on the loan page itself!

8) Surprisingly, you shouldn't worry too much about the credit grade itself. The major exception to this is if you're investing from a fixed income, in which case you'll want to keep to higher credit grades.

9) What data should you look for? Look for loans with no current delinquencies (allow one if they provide a good reason for it), and less than 3 delinquencies in the past year. Also, a debt-to-income ratio of less than 40% is a must.

10) Many of these tips can be looked for in a "saved search", so you can look for them with just one click! You may want to create several saved searches, and compare their results. If you see the same loan over several searches, it is more likely to be a good

candidate for you. I generally look for a 14-15% or lower risk-adjusted return when using a saved search.

11) I stop bidding on a loan once it goes below a 14% interest rate.

12) Give preference to "Automatic Funding Loans". These are loans whose interest rates won't change, and which end when they are fully funded. Strangely, you'll still be asked to enter an interest rate bid, so enter 0%. You'll still get the promised interest rate, but you won't be kicked off the loan by someone who, mistakenly or purposefully, enters an interest rate lower than the loan.

Finally, do keep in mind that these are real loans, and there is real risk involved. As with any investment in which there is risk involved, only risk money which you can afford to lose.

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About Author

Scott Cram has been a Prosper.com investor for a full year now, averaging 21.33% interest on his loans, as mentioned in the above article.

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