

## **Quadrant II – Notes**

**Programme:** B. Sc. (Hons.) Agri.

**Subject:** Agricultural Economics

**Course Code:** ECON-242

**Course Title:** Agricultural Finance and Cooperation

**Module Name:** Repayment Plans

**Module No:** 6

**Name of the Presenter:** Dr. Rachana Kolambkar

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### **Notes :**

The repayment of term loans (i.e. medium term loans and long term loans) differs from that of short term loans because they are characterized by their partially liquidating nature. These loans are recovered by a given number of instalments depending up on the nature of the asset and the amount advanced for the asset under consideration.

There are six types of repayment plans for term loans and they are

1. Straight-end repayment plan/single repayment plan/lumpsum repayment plan
2. Partial repayment plan or Balloon repayment plan
3. Amortized repayment plan
  - a) Amortized decreasing repayment plan
  - b) Amortized even repayment plan or Equated annual instalment method
4. Variable repayment plan (or) Quasi-variable repayment plan
5. Optional repayment plan
6. Reserve repayment plan (or) Future repayment plan

### **1. Straight-end Repayment Plan or Single Repayment Plan**

The entire loan amount is to be cleared off after the expiry of stipulated time period. The principal component is repaid by the borrower at a time in lumpsum when the loan matures, while interest is paid each year.

### **2. Partial repayment plan or Balloon repayment plan**

Here the repayment of the loan will be done partially over the years. Under this repayment plan, the instalment amount will be decreasing as the years pass by except in the maturity year (final year), during which the investment generates sufficient revenue. This is also called as balloon repayment plan, as the large final payment made at the end of the loan period (i.e. in the final year) after a series of smaller partial payments.

### **3. Amortized repayment plan:**

Amortization means repayment of the entire loan amount in a series of instalments. This method is an extension of partial repayment plan. Amortized repayment plans are of two types

#### **a) Amortized decreasing repayment plan**

Here the principal component remains constant over the entire repayment period and the interest part decreases continuously. As the principal amount remains fixed and the interest amount decreases, the annual instalment amount decreases over the years. loans advanced for machinery and equipment will fall under this category. As the assets do not require much repairs during the initial years of loan repayment, a farmer can able to repay larger instalments.

#### **b) Amortized even repayment plan**

Here the annual instalment over the entire loan period remains the same. The principal portion of the instalment increases continuously and the interest component declines gradually. This method is adopted for loans granted for farm development, digging of wells, deepening of old wells, construction of godowns, dairy, poultry units, orchards etc.

The annual instalment is given by the formula

$I = B * i / 1 - (1+i)^{-n}$  Where I= annual instalment in Rs.

B= principal amount borrowed in Rs.

n= loan period in years

i= annual interest rate

#### **4. Variable repayment plan or Quasi-variable repayment plan**

As the name indicates that, various levels of instalments are paid by the borrower over the loan period. At times of good harvest, a larger instalment is paid and at times of poor harvest smaller instalment is paid by the borrower. Hence, according to the convenience of the borrower the amount of the instalment varies here in this method. This method is not found in lending's of institutional financial agencies.

#### **5. Optional repayment plan:**

Here in this method an option is given for the borrower to make payment towards the principal amount in addition to the regular interest.

#### **6. Reserve repayment plan or Future repayment plan**

This type of repayment is seen with borrowers in areas where there is variability in farm income. In such areas the farmers are haunted by the fear of not paying regular loan instalments. To avoid such situations, the farmers make advance payments of loan from the savings of previous year. This type of repayment is advantageous to both the banker and borrower. The bankers need not worry regarding loan recovery even at times of crop failure and on the other hand borrower also gains, as he keeps up his integrity and credibility.