Loans

How have wealthy people made money?
Borrowed and invested – repeatedly.
(Many with timing and luck)

Topics
- Types of Loans
- Amortization
  - Principal and Interest
- Other Costs
- Lenders
- Comparing Loans

Types of Credit
- Line of Credit
  - Revolving, credit card
- Short Term
  - 90 day operating loan
- Intermediate
  - Cows, machinery, auto (3-7 years)
- Long Term
  - Land, buildings, homes (15-30 years)

Types of Loans
- Interest on Balance
  - Fixed Term – 15 or 30 yrs
- Adjustable Rate (ARM)
  - 5/1, 3/1, 1/1
- Balloon
- Interest Only

Interest Rates
The Prime Rate is the interest rate charged by banks to their most creditworthy customers

The federal funds rate is the cost of borrowing immediately available funds, primarily for one day.
Amortization

- Amortizing
  - Equal payments throughout
  - Interest, Principal, Balance
  - Interest first, then Principal
- All the parts add up
  - Interest = Payments – Principal
  - Principal = Payments – Interest
  - Principal = Bal (pmt i-1) – Bal (pmt i)

Loan PMT, INT, & PRN

Prepayment/Acceleration

- Prepayment – available?/important?
- Acceleration Schedule
  - Paying extra – regularly or intermittently
  - What is saved?
  - Paying every other week on a 30 yr mortgage will extinguish debt in 18-19 yrs
  - Be disciplined

Various and Sundry Costs

- See Property Buying.xls
- Loan Initiation Fee
- Points
  - How much, when, who, why?
- Locking Rates
- The application – Be Prepared!!
- Closing Costs + Prepaid Expenses

Where to Look?

- Newspaper
- Internet
- Realtors
- Banks

Let’s Amortize!
Ag Lenders
- Commercial Banks (40%)
- Farm Credit Services (25%)
- Individuals (23%)
- Farm Services Admin (FmHA) (6%)
- Others (6%)

Other Thoughts
- Shop Around
- Negotiate Credit Terms
- Borrow for needs, not wants
- Do not owe on highly depreciable items
- Use insurance to manage risk

Comparing Loans
- Interest & Points
- Interest Rate
- Present Value

Five Cs of Credit
- Character
  - Sound character and management ability?
  - Honesty, integrity, self-discipline, future planning, manage profitable operation (FS)
- Capital
  - Financial position
  - Working capital, liquidity, and debt structure
- Capacity
  - Repay new debt, meet current obligations, provide adequate return, capital replacement

Borrower-Lender Relationship
- What to look for when selecting a lender
  - Understands your industry
  - Long term presence in industry
  - Capacity to meet your needs
  - Competitive loan products
  - Experiences employees
  - Access to the decision maker
  - More than just a transaction
  - Ethical and trustworthy
  - Process requests in a timely manner
  - Communicates terms, rates, and conditions (up-front)

Other Thoughts
- Shop Around
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Five Cs of Credit
- Collateral
  - Liquidated for repayment
- Conditions
  - Purpose of loan, loan amount, terms of repayment
  - Weight given to each factor varies
  - Weaknesses in one factor may be offset by strengths in another

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Comparing Loans
- Interest & Points
- Interest Rate
- Present Value

Compare some!
Borrower-Lender Relationship

- How to be a valuable partner in the lending relationship
  - Provide accurate financial information
  - Provide a business plan
  - Maintain an honest and ethical relationship
  - Maintain open and regular communication with your lender

Summary

- Shop around
- Plan ahead
- Negotiate
- Borrow for needs, not wants
- Stay within the plan
- Do not owe on highly depreciable items
- Borrow for high, probable returns
- Use insurance to manage credit risks
- You can control those credit cards