Institutions providing home loans intermittently come up with new forms of loans that are devised to meet the needs of house buyers from every section of the society. However, before choosing a particular loan, it is very important to have a comprehension about the most important constituent of the loan - the EMIs.

An EMI, or equated monthly instalment, is a certain amount of money that is payable by you to the bank (in case you have taken a home loan) in order to obtain legal possession of the house.

**What is an EMI?**

In plain financial terms, an EMI is the amount of money paid by borrowers, each calendar month, to the lender, for clearing their outstanding loan. This also means that a sum of money gets deducted from your particular account irrespective of any sudden untoward financial stringency faced by you. EMI payments are made every month, generally on a fixed date, for the entire tenure of the loan, till the outstanding amount has been completely repaid.

**EMI break-up**

When it comes to segregating the sum that is payable towards the loan, EMI is actually deduced based on an unequal combination of principal and interest. In the initial years of the loan, a major portion of the EMI comprises the interest payable by the borrower. As the loan matures, and as the principal gradually gets paid, the outstanding loan amount reduces. The interest component thus becomes lower than the principal, and finally minimal. The EMI, though, stays as a constant amount each month, except in the following cases:

Instances when the borrower paid a lump sum amount of the outstanding loan, then this amount gets duly adjusted against the remaining balance, thereby reducing the EMI. Now, in this particular case, the borrower gets an option where he/she can maintain the EMI while reducing the loan tenure.

In case the borrower has opted for floating rate of interest, then the EMI varies according to market fluctuations.
The EMI of your home loan is determined by four major factors

1. **Principal amount**: The principal amount refers to the actual sum of money that is borrowed by the lender. Beyond question, the principal amount is a major determining factor towards the EMI that is to be paid by you.

2. **Rate of interest**: The rate of interest is the rate at which the borrower has taken money from an organization or market. This is the most important factor when it comes to determining your EMI. The higher the rate of interest, the greater is the EMI payable by you. It is always advisable to do a market study of various interest rates offered by lending bodies and then decide upon a particular product.

3. **Loan tenure**: The tenure of the loan refers to the duration for which the loan has been taken. The longer the duration of the loan, the lesser the monthly EMI burden on the borrower.

4. **Method of computation**: The method that is adopted to calculate the EMI is a crucial factor when it comes to determining the EMI payable by you. The various methods adopted are:
   
   a. **Annual reducing method**: In this method of EMI calculation, although the EMI is paid by the borrower at the end of every month, the principal amount and the rate of interest is made at the end of the year. This type of EMI calculation has a huge disadvantage attached to it, as the borrowers continue to pay interest on a portion of the principal that has already been paid back to the lender.
   
   b. **Monthly reducing loans**: This is a better and easy-to-understand method of EMI calculation and is usually the most common calculation method adopted. In this calculation methodology there is a reduction in principal with EMI being paid every month. The interest is calculated on the outstanding balance.
   
   c. **Daily reducing loans**: As the name implies, in this method the principal reduces every day, with daily loan repayments. The interest is charged on the outstanding balance. However, daily EMI payment is not a very feasible option; hence this method is not a very popular method.
**Loan amortization schedules**

A loan amortization schedule is a product that contains home loan information such as period of scheduled payments, amount borrowed and amount outstanding. It also gives a detailed breakup of every EMI towards repayment of interest and the outstanding principal of the loan. The amortization table is prepared with the use of financial mathematics by financial institutions. It helps borrowers make vital decisions about their loan, on prepayment or refinance. It also provides details of interest for tax related benefits.

**Step up and step down EMI**

EMIs are at times planned according to the expected increase and decrease in the salary of the borrower.

In step up EMI, the EMI is gradually increased on the premise that the salary of the borrower will increase in the future. In this system, the initial EMI charged is less, and it increases as the expected income of the borrower increases. The change in EMI would be done twice during the entire loan tenure.

Similarly, in the case of step down EMI, the initial EMI charged is substantially higher and it gradually reduces with the number of payments done.

**Pre-EMI and advance disbursements**

There are instances where the borrower may opt for a partial disbursement of their home loan on the basis of the stages of construction of their house. In such cases, a pre-EMI is to be paid every month till the final loan is disbursed. The real loan repayment would commence only after the entire loan is disbursed. This pre-EMI would, therefore, comprise only the interest accrued on the disbursed money.

Also, there are cases when the entire loan may be disbursed by lenders before the completion of house construction. This is known as an advance disbursement and is undertaken by the lender when it is requested by the borrower and the lender is convinced of the capabilities of the builder to complete the construction work in time.

In these cases, the EMI payment starts immediately from the date of disbursement.

**Fixed and floating rate of interest**

EMIs can be calculated either on a fixed or a floating rate of interest.
Fixed rate of interest: A fixed rate of interest is charged throughout the loan tenure, thereby making the EMI payable a constant sum. It is generally better to opt for a fixed rate only when the prevailing interest rates have reached rock bottom levels and if an upward trend is anticipated.

Floating rate of interest: Floating rates vary with the market lending rates and are thus prone to fluctuations. The EMI would increase or decrease depending on the interest rate movement. In this case, banks provide an alternative to increase the tenure of the loan, at a constant EMI, for borrowers who do not desire their EMI to be increased in case of higher interest rates.